

**A COMPARATIVE STUDY OF TAX INCENTIVES FOR SMALL BUSINESSES
AND INVESTORS IN SMALL BUSINESSES IN SOUTH AFRICA, AUSTRALIA,
NEW ZEALAND, SINGAPORE AND IRELAND**

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ABSTRACT

In the South African context, it is accepted that small businesses will be the vehicle for job creation and changing the current business ownership patterns. This is to be achieved by creating access to finance, exploring the role of venture capital and simplifying the tax obligations and the compliance burden. The literature indicates that the current South African tax incentives for small businesses are perceived as unfair and fundamentally ineffective. The objective of this thesis was to compare the tax incentives available to small businesses and investors in small businesses in South Africa to those available in Australia, New Zealand, Singapore and Ireland, in order to identify possible measures that could be introduced in South Africa.

In addressing the objective, the research set out to provide, in terms of South African tax legislation, a definition of a small business for tax purposes and document the tax incentives available for start-up and existing small businesses, as well as the tax incentives available for investors in small businesses, either through a venture capital company or a direct investment in small business. It was found that South Africa has a complex and onerous multi-layered approach to classifying a taxpayer as either a “micro business” or a “small business corporation” for the purpose of applying tax incentives. The international jurisdictions included in this research follow a single requirement approach, based on either one or a combination of turnover, balance sheet total or staff headcount. The international jurisdictions provide a wide range of tax incentives to small businesses and investors in small businesses, aimed at reducing taxable income to enable the small businesses to grow and access equity finance. By identifying differences and similarities, a number of possible tax relief measures were recommended that could be introduced in South Africa.

Key words: taxation, incentives, micro business, small business, small business corporation, small business entity, tax relief.

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CHAPTER 1: INTRODUCTION

1.1 CONTEXT OF THE RESEARCH

According to the National Planning Commission in the *National Development Plan: Vision for 2030* (2011: 140):

Small and expanding firms will become more prominent, and generate the majority of new jobs created. They will also contribute to changing apartheid legacy patterns of business ownership. They will be stimulated through public and private procurement, improved access to debt and equity finance, and a simplified regulatory environment.

It is clear that the National Development Plan aims to encourage the growth of small and medium-sized businesses in South Africa. One of the key proposals suggested to support the development of small and medium-sized business is “access to ... finance and exploring the role of venture capital”, as well as to “simplify regulations in relation to tax” (National Planning Commission, 2011: 142-143).

The South African Institute of Chartered Accounts (SAICA, 2015: 8) reports that one of the main barriers to starting a business in almost all developing countries is the difficulty in obtaining finance:

This holds true for South African Small and Medium Enterprises, where this is considered the second most difficult barrier when starting a new business. In South Africa, red tape from government is considered to be the biggest obstacle. Compliance with legislation and registering for VAT are also significant obstacles.

For the purposes of the present study, two obstacles encountered by South African small businesses in relation to taxation will be examined: the income tax relief available to small businesses and the tax relief available for investors in small businesses.

Aucamp (2011: 1) compiled “a comparative study of tax relief measures for Small Medium and Micro Enterprises (SMMEs) in South Africa and Australia”. The author chose Australia as the comparative country, due to their recent implementation of Small, Medium and Micro

Enterprise tax legislation at the time of the study. Aucamp (2011) analysed the definition of Small, Medium and Micro Enterprises, identified the tax relief available in South Africa and Australia and critically compared the tax relief provided in the two countries. Aucamp (2011: 58) concluded that in South Africa the tax provisions for SMMEs are complicated, the compliance cost high and the requirements to be classified as an SMME for tax purposes narrow. In Australia, however, “most of the tax relief measures were included in the Australian legislation to reduce compliance cost for SMMEs”. In the comparative study, Aucamp also evaluated the venture capital incentives available in Australia and South Africa at the time of the study. Aucamp (2011: 55) concluded that Australia uses tax incentives to reward successful investments in small business, while South Africa provides a tax deduction for the acquisition of an equity interest in the business.

A study by Mkhize (2011) included an analysis of the section 12J venture capital provisions in the Income Tax Act, No. 58 of 1962 (the South African Income Tax Act), and Mkhize (2011: 59) concluded that:

The venture capital incentive legislation will be effective given that it allows for deduction of expenditure actually incurred in the acquisition of shares. The venture capital incentives for small business will facilitate access to finance by small businesses in mining and other high tech industries.

As part of a study, du Toit (2012: 79) included a high-level examination of venture capital incentives available in Manitoba and British Columbia in Canada and concluded that:

Section 12J may be extended to include a deduction where investments are made directly in qualifying small businesses. This will be similar to the incentive available in the Manitoba province in Canada. This will encourage investment by companies directly into small businesses and not just investments via a venture capital company.

Stols (2014) examined the effectiveness of the small business tax relief measures in South Africa and concluded (2014: 62):

It is clear from the study that current small business tax relief measures contained in section 12E of the Income Tax Act and Turnover Tax could contribute significantly towards the

growth and success of small business. These tax relief measures are currently not meeting all the objectives as set out by SARS. The positive contribution of these tax relief measures toward the growth of small business is limited and could be further improved to ensure all objectives are met and benefits for small businesses are increased.

Gluckman (2013: 7) evaluated “the perceived fairness of the current Turnover Tax system” (Schedule 6 to the South African Income Tax Act) and found that:

The Turnover Tax system, in its current format, is not being perceived as completely fair. Although the Turnover Tax system is currently a workable tax system, SARS should consider making changes to the legislation in order to support the growth and development of small businesses within South Africa.

The Davis Tax Committee report: *Small and Medium Enterprises: Second and Final Report* (2016: 5), asserts that “the Turnover Tax package is sufficient for the time being”. Gluckman (2013), however, found that the Turnover Tax package “is not being perceived as completely fair”.

Evans, Hansford, Hasseldine, Lignier, Smulders and Vaillancourt (2014: 475) concluded that “based upon the evidence that is available, it does appear that the Small Business Tax Concessions may not be as effective as one would have hoped and is therefore an area that requires specific revenue authority/treasury attention”. The Davis Tax Committee (2016: 6) has drawn attention to the fact “that the Small Business Corporation tax system is fundamentally ineffective”. This conclusion is similar to that of Aucamp (2011), Mhize (2011) and Stols (2014).

As indicated in the *National Development Plan: Vision for 2030* “small and expanding firms will become more prominent and generate the majority of new jobs created” (National Planning Commission, 2011: 140), but the literature indicates that the current tax relief measures are not meeting the objectives of simplifying the regulation of and assisting the growth of small business in South Africa.

Therefore, it is necessary to establish small business tax relief measures that are available in other countries to assist South Africa, to “simplify regulations in relation to small business tax” (National Planning Commission, 2011: 142-143) and provide support for small businesses in South Africa.

Du Toit (2012: 1), in her study, aimed to “offer a conclusion as to whether tax incentives for Small and Medium Enterprises in South Africa are comparable to those available in Australia and Canada for similar organizations”. Du Toit (2012) chose Australia and Canada, based on the fact that “information published in the Survey on the Taxation of Small and Medium-sized enterprises by the OECD highlighted that the taxation policies regarding SMEs in Australia and Canada are similar to those in South Africa”. This study concluded that: “the tax incentives in South Africa are on par with those of the developed countries such as Australia and Canada”. Australia was therefore selected for the present research.

The World Bank Group in *Doing Business 2016, Measuring Regulatory Quality and Efficiency* (2016: 1) “focuses on regulations and regulatory processes involved in setting up and operating a business”. The World Bank Group (2016: 19) “measured aspects of business regulation affecting domestic small and medium-size firms in 11 areas across 189 economies”. The 2016 report ranked Singapore number one and New Zealand number two based on the ease of doing business.

Small and Medium Enterprises accounted for 99.8% of all active business enterprises in the Republic of Ireland in 2014 (Central Statistics Office, 2016: Online). The Irish government recently amended specific provisions in relation to small business taxation in both their 2015 and 2016 Budget. The 2015 Budget, together with other provisions, introduced amendments to the Employment Investment Incentive Scheme and the Seed Capital Scheme, in an attempt attract investments in small business (Irish Tax Institute, 2014: Online). The 2016 Budget introduced “a number of measures aimed at encouraging entrepreneurship and supporting small business owners” by extending the three-year tax relief from corporation tax, introducing a tax credit for the self-employed entrepreneurs and increasing the Entrepreneurs’ Capital Gains Tax relief (Irish Tax Institute, 2015: Online).

It is submitted that a comparative analysis between South African small business tax relief provisions and those of countries that recently amended their legislation to provide greater

access to tax concessions for small business (Ireland) and top ranked countries in respect of the ease of doing business (Singapore and New Zealand) should provide the opportunity to comment on the similarities and differences in respect of tax relief for small businesses and the investors in small businesses, and identify incentives that could be implemented in South Africa.

1.2 GOALS OF THE RESEARCH

The goal of this research is to compare the tax incentives available to small businesses and investors in small businesses in South Africa to those available in Australia, New Zealand, Singapore and Ireland, to identify possible measures to be introduced in South Africa. In addressing the goal, the research sets out to address the following sub-goals in relation to all the jurisdictions involved in the research:

- the definition of a small business for tax purposes;
- the tax incentives available for start-up and existing small businesses;
- the tax incentives available to investors in small businesses, either through a venture capital company or a direct investment in a small business;
- possible measures that could be introduced in South Africa.

1.3 METHODS, PROCEDURES AND TECHNIQUES

An interpretative research approach is adopted, as this method seeks to both understand and describe (Babbie & Mouton: 2009). The research methodology applied can be described as a *doctrinal* research methodology. The doctrinal research methodology involves “the systematic process of identifying, analysing, organising and synthesising statutes, judicial decisions and commentary” (McKerchar, 2008: 18-19). Furthermore, the doctrinal research methodology analyses the relationships between rules, explains areas of difficulty and is based purely on documentary data (McKerchar: 2008). “Comparative law, which compares the legal systems of different countries, falls into this research methodology” (Stack, 2013: 34).

The documentary data used for this research consists of:

- legislation in the form of the Tax Acts of the countries included in the research;
- Interpretation Notes, Notices, Regulations and similar pronouncements relating to small businesses, issued by the Revenue Services in the countries included in the research; and
- textbooks and other writings.

The research is conducted in the form of an extended argument that is supported by documentary evidence. The validity and reliability of the research and the conclusions is ensured by:

- adhering to the rules of the statutory interpretation, as established in terms of statute and common law;
- placing greater evidential weight on legislation and the writings of acknowledged experts in the field;
- discussing opposing viewpoints and concluding, based on a preponderance of credible evidence; and
- the rigour of the arguments.

The research only involves the analysis of documentary data. As all data used for this research are publicly available, no ethical considerations arise in relation to their use.

1.4 OVERVIEW OF THE CHAPTERS

Chapter 2 considers the sub-goals of defining a small business for tax purposes, the tax incentives available for start-up and existing small businesses, and the tax incentives available to investors in small businesses, either through a venture capital company or a direct investment in a small business in a South African context. In chapter 3, these sub-goals are addressed as they relate to Australia, New Zealand, Singapore and Ireland. Chapter 4 provides a comparison of the definition of a small business, the incentives available to a small business and investors in these businesses. The comparison is made between South Africa and Australia, New Zealand, Singapore and Ireland. Chapter 4 identifies the differences and similarities between

South Africa and the international jurisdictions and concludes by providing possible measures that could be introduced in South Africa. Chapter 5 concludes this thesis, by highlighting the research goals, summarising the main conclusions reached in each chapter, identifying the limitations of scope and opportunities for future research.

CHAPTER 2: TAX RELIEF MEASURES FOR SMALL, MEDIUM AND MICRO ENTERPRISES IN SOUTH AFRICA

2.1 INTRODUCTION

In addressing the first three sub-goals of the research: defining a small business for tax purposes, identifying the tax incentives available for start-up and existing small businesses and the tax incentives available to investors in small businesses, this chapter provides definitions of small, medium and micro-sized enterprises for South African income tax purposes and identifies and discusses the tax incentives available for these small businesses and investors in small businesses in South Africa

2.2 SMALL, MEDIUM AND MICRO-SIZED ENTERPRISE

Evans et al (2014: 456) submit that “there is no universally accepted definition of small business. Moreover, the definition of a small business for the purpose of tax concessions may vary even within the same jurisdiction between taxes”. Section 1 of the South African Income Tax Act defines a “small, medium or micro-sized enterprise” as “any person that qualifies as a micro business as defined in paragraph 1 of the Sixth Schedule or any person that is a small business corporation as defined in section 12E(4)”. The remainder of the discussion examines the requirements contained in the South African Income Tax Act in relation to a:

- “micro business” in terms of the Sixth Schedule;
- “small business corporation” in terms of section 12E(4);
- “small business” in terms of paragraph 57 of the Eighth Schedule, as paragraph 57 and 57A provides capital gains tax relief for the disposal of small and micro business assets; and
- investments in a “venture capital” company in terms of section 12J.

2.3 MICRO BUSINESSES

The Tax Guide for Micro Businesses 2016/17 (issue 2) (SARS, 2017a: 12) indicates that “the turnover tax system is mainly aimed at benefiting micro businesses that actively engage in labour intensive entrepreneurial business activities”. SARS (2017a: 2) observes that:

In order to alleviate the tax compliance burden on micro enterprises, a turnover tax regime was introduced... It streamlines the tax compliance process for micro businesses by replacing a registered micro business’ liability for income tax (including Capital Gains Tax) and, to an extent, dividends tax, with a liability to account for turnover tax.

2.3.1 THE DEFINITION OF A MICRO BUSINESS

A “micro business” is defined in terms of paragraph 1 of the Sixth Schedule to the South African Income Tax Act (the Sixth Schedule) as “a person that meets the requirements set out in Part II of this Schedule”. In terms of, paragraph 2, Part II of the Sixth Schedule to the South African Income Tax Act:

- (1) A person qualifies as a micro business if that person is a —
 - (a) natural person (or the deceased or insolvent estate of a natural person that was a registered micro business at the time of death or insolvency); or
 - (b) company,
where the qualifying turnover of that person for the year of assessment does not exceed an amount of R1m.

- (2) If a person described in subparagraph (1) carries on a business during the relevant year of assessment for a period which is less than 12 months, the amount described in subparagraph (1) is reduced proportionally taking into account the number of full months that it did not carry on business during that year.

Therefore, the turnover tax regime is an option for persons conducting their business as sole proprietors, partnerships, close corporations, co-operatives or private companies.

Before proceeding to discuss the tax incentives available to a micro business, it is important to examine the term “qualifying turnover”. It is submitted that this term forms a key part of the

“micro business” definition. In terms of paragraph 1 of the Sixth Schedule “qualifying turnover” is defined as:

- the total receipts from carrying on business activities, excluding any —
- (a) amount of a capital nature; and
 - (b) amount exempt from normal tax in terms of section 10(1)(zK) or 12P.

Amounts of a capital nature; amounts received from a small business funding entity (section 10(1)(zK)) and amounts received in respect of government grants (section 12P) are not taken into account when calculating “the total receipts” taken into account when calculating the “qualifying turnover”. The Tax Guide for Micro Businesses 2016/17 (issue 2) (SARS, 2017a: 4) notes that to calculate “qualifying turnover”, “it is immaterial whether a receipt constitutes ‘gross income’ or is in fact taxable”, and where a micro business is voluntarily registered for Value-Added Tax (VAT), the amounts included in taxable turnover will include VAT, where VAT was charged on the supply of the goods or services.

The phrase “carrying on business activities” is not defined in the South African Income Tax Act. In *Cape Town Municipality v Clarensville (Pty) Ltd*, 1974(2) All SA 346 (C), Baker J stated (at 357) that “carrying on business activities” means:

- an act of selling or supplying goods or services and an intention to continue selling or supplying such goods or services as and when the opportunity arises for as long as it is thought desirable; or
- a series of acts of selling or supplying goods or services in circumstances from which this intention can be inferred.

In terms of paragraph 13 of the Sixth Schedule, the “qualifying turnover” of the person seeking to register as a “micro business” may be combined with the receipts of connected persons if:

- the connected person carries on business activities that should properly be regarded as forming part of the business activities carried on by that person; and
- the main reason or one of the main reasons for “splitting” the business activities is to ensure that the qualifying turnover of that person is below the qualifying turnover threshold.

It can be concluded that none of the connected persons will qualify as a “micro business” where the combined “qualifying turnover” of all the connected persons in relation to the person trying to register as a “micro business”, exceeds R1m.

The indications are therefore that:

- only receipts and not accruals will be taken into account when calculating “qualifying turnover”;
- amounts of a capital nature, amounts received from small business funding entities and government grants are not included in “qualifying turnover”; and
- only receipts from “carrying on business activities” are taken into account when calculating “qualifying turnover”.

The Tax Guide for Micro Businesses 2016/17 (issue 2) (SARS, 2017a: 2) notes that:

... certain receipts and income streams of a micro business could be taxable under the normal tax system. These receipts and income streams may relate to remuneration and investment income received by the micro business, as well as amounts derived by the micro business from carrying on business activities outside South Africa.

Having examined the requirements to be classified as a “micro business”, the factors that may exclude a person from being classified as a “micro business”, are now discussed.

In terms of paragraph 3 of the Sixth Schedule to the South African Income Tax Act, a person cannot register as a “micro business” for a “year of assessment” where:

- the person holds non-permissible shares in terms of paragraph 4 of the Sixth Schedule to the South African Income Tax Act;
- the receipts from “professional service” exceeds 20% of total receipts for a natural person (or the estate of the deceased or insolvent person) or “investment income” and “professional service” receipts exceeds 20% of the total receipts of a company;
- the person is a “labour broker” without an exemption certificate or a “personal service provider”; and

- the total amounts from the disposal of immovable property or other assets used for business purposes (excluding financial instruments) for the current and immediate preceding two years of assessment exceeds R1.5m in total;
- in addition, a company cannot register as a “micro business” where:
 - the “year of assessment” does not end on the last day of February;
 - any holder of shares, at any time during the “year of assessment” was not a natural person (or the estate of the deceased or insolvent person);
 - any holder of shares held non-permissible shares (with the exception of shares held in a dormant company and the market value of all assets during any “year of assessment” did not exceed R5 000 or the company “has taken steps to liquidate, wind up or deregister”); and
 - the company is a tax exempt Public Benefit Organisation in terms of section 30 of the South African Income Tax Act, a recreational club in terms of section 30A of the South African Income Tax Act or an association in terms of section 30B of the South African Income Tax Act;
- a partner in a partnership cannot register as a “micro business” where:
 - any one partner is not a natural person;
 - the partner is a partner in more than one partnership “at any time of that year of assessment”; or
 - the partnership “qualifying turnover” exceeds R1m.

The prohibitions set out in paragraph 3 of the Sixth Schedule introduce the terms “professional service”, “personal service provider” and “investment income” to describe a person that will not qualify as a “micro business”. Before proceeding to examine the income tax incentives available for a “registered micro business”, it is important to discuss the three terms.

Paragraph 1 of the Sixth Schedule defines a “professional service” as:

A service in the field of accounting, actuarial science, architecture, auctioneering, auditing, broadcasting, consulting, draftsmanship, education, engineering, financial service broking, health, information technology, journalism, law, management, real estate broking, research, sport, surveying, translation, valuation or veterinary science.

A “personal service provider” is defined in paragraph 1 to the Fourth Schedule of the South African Income Tax Act as:

- a company or trust;
- where a person connected to the company or trust provides the service to a client; and
 - where the services are provided directly to the client, the connected person could be regarded as an employee of the client;
 - the services are provided “mainly at the premises of the client”, “subject to the control and supervision of the client as to the manner in which duties are performed”; or
 - “more than eighty percent of the income of the company or trust” is derived “directly or indirectly from any one client” during a “year of assessment”.

A company or a trust will not be considered a “personal service provider” if the company or trust employed at least three full-time employees “throughout the year of assessment”, provided that the employees are not “a holder of a share in the company, a settlor or beneficiary of the trust, or a connected person in relation” to a holder of a share, a settlor or beneficiary.

“Investment income” is defined in terms of paragraph 1 of the Sixth Schedule as:

- (i) any income in the form of annuities, dividends, interest, rental derived in respect of immovable property, royalties, or income of a similar nature; and any proceeds derived from the disposal of financial instruments.

It is clear, therefore, that receipts from “professional services”, a “personal service provider” and “investment income” exclude certain persons from registering as a “micro business” and exclude certain types of income from qualifying for the turnover tax concessions.

Paragraph 4, read with paragraph 3(a) and 3(f)(iii) of the Sixth Schedule, permits the holder of shares in, or a member of a “micro business” to hold the following shares or interest in:

- a company listed on the JSE;
- “any investment scheme carried on outside South Africa, that is comparable to” a portfolio in a collective investment scheme in bonds, securities or “a portfolio in a

collective investment scheme in property” (classified as a Real Estate Investment Trust);

- any of the following companies:
 - a body corporate established under the Sectional Titles Act No 95 of 1986;
 - a share block company established under the Share Block Control Act No 59 of 1980; and
 - an “association of persons managing the collective interests common to all members”;
- less than five percent of the interest in a social, consumer, burial society, or similar co-operative;
- less than five percent of the interest in a primary savings or primary savings and loans co-operative bank;
- a venture capital company in terms of section 12J of the South African Income Tax Act; or
- a Friendly Society in terms of section 1 of the Friendly Societies Act No 25 of 1956.

2.3.2 INCOME TAX INCENTIVES AVAILABLE TO REGISTERED MICRO BUSINESSES

A “registered micro business”, is a “micro business” registered in terms of paragraph 8 of the Sixth Schedule. In terms of section 48A of the South African Income Tax Act, “turnover tax” is calculated on “taxable turnover” for the “year of assessment” by a “registered micro business”. Paragraph 5 of the Sixth Schedule, defines “taxable turnover” as:

The taxable turnover of a registered micro business in relation to any year of assessment consists of all amounts not of a capital nature received by that registered micro business during that year of assessment from carrying on business activities in the Republic, including amounts described in paragraph 6 and excluding amounts described in paragraph 7, less any amounts refunded to any person by that registered micro business in respect of goods or services supplied by that registered micro business to that person during that year of assessment or any previous year of assessment.

The Sixth Schedule provides for specific inclusions in “taxable turnover” in terms of paragraph 6, whereas paragraph 7 of the Sixth Schedule provides for specific exclusions from “taxable

turnover”. Paragraph 6 of the Sixth Schedule to the South African Income Tax Act states that the following amounts are specifically included in “taxable turnover”:

- Fifty percent of all receipts of a capital nature from the disposal of –
 - immovable property mainly used for business purposes, other than trading stock; and
 - any other asset mainly used for business purposes, other than any financial instrument.
- Investment income, other than dividends and foreign dividends, received by a company.

In terms of paragraph 7 of the Sixth Schedule the following amounts are specifically excluded from “taxable turnover”:

- investment income derived by a natural person;
- amounts received from a small business funding entity or government grants, which are exempt from normal tax;
- taxable amounts accrued to the business, before registering as a “micro business”;
- refunds “in respect of goods or services” supplied to the “micro business”.

Section 48B of the South African Income Tax Act provides that “the rates of tax chargeable in terms section 48A must be fixed annually by Parliament”. The Tax Guide for Micro Businesses 2016/17 (issue 2) (SARS, 2017a: 2) has drawn attention to the fact that the term “turnover tax” suggests that the registered micro business’ tax liability is determined by applying a specific turnover tax rate to the registered micro business’ “taxable turnover” in a particular year of assessment. Table 2.1 sets out the rates applicable for the “year of assessment” ending 28 February 2018.

Table 2.1: Turnover Tax Rates - 1 March 2017 to 28 February 2018

| Taxable turnover (R) | Rate of tax (R) |
|-----------------------------|--|
| 0 – 355 000 | 0% |
| 335 001 – 500 000 | 1% of the amount above 335 000 |
| 500 001 – 750 000 | 1 650 + 2% of the amount above 500 000 |
| 750 001 and above | 6 650 + 3% of the amount above 750 000 |

Source: SARS (2017b: online)

The “turnover tax” regime also provides for administrative concessions in the form of interim payments and record keeping. In terms of paragraph 11 of the Sixth Schedule, a “registered micro business” is required to make two interim payments based on an estimated “taxable turnover” and a final payment in instances where the assessed “turnover tax” based on actual “taxable turnover” exceeds the two interim payments. The first interim payment must be made within six months from the beginning of the “year of assessment”. The amount to be paid is calculated as fifty percent of the “turnover tax” calculated on an estimation of the “taxable turnover” for the full “year of assessment”. The Tax Guide for Micro Businesses 2016/17 (issue 2) (SARS, 2017a: 27) explains that “this estimate must not be less than the micro business’ taxable turnover for the previous year of assessment, unless the micro business applies to SARS and SARS, having regard to the circumstances of the case, approves a lower estimate”.

The second interim payment must be made on or before the last day of the year of assessment. The amount to be paid is calculated as 100% of the turnover tax on an estimation of the “taxable turnover” for the full “year of assessment” less the first interim payment made.

In terms of paragraph 14 of the Sixth Schedule, a “registered micro business” must only retain a record of:

- (a) amounts received by that registered micro business during a year of assessment;
- (b) dividends declared by that registered micro business during a year of assessment;
- (c) each asset of that registered micro business as at the end of a year of assessment with a cost price of more than R10 000; and
- (d) each liability of that registered micro business as at the end of a year of assessment that exceeded R10 000.

The provisions in terms of paragraph 14 of the Sixth Schedule apply, notwithstanding the provisions relating to returns and records in terms of Part A of Chapter 4 of the Tax Administration Act, No 28 of 2011 (the South African Tax Administration Act). In terms of section 29(3) of the South African Tax Administration Act, the records must be retained for “a period of five years from the date of the submission of the return”.

2.3.3 CAPITAL GAINS TAX RELIEF

In terms of paragraph 57A of the Eighth Schedule to the South African Income Tax Act (the “Eighth Schedule”) “a registered micro business as defined in terms of the Sixth Schedule must disregard any capital gain or capital loss in respect of the disposal by that business of any asset used mainly for business purposes”. The word mainly is not defined in the South African Income Tax Act, but de Koker and Williams (2017: §24.101A) have drawn attention to the fact that “the word ‘mainly’ establishes a purely quantitative measure of ‘more than fifty percent’, and presumably an asset would be regarded as being used mainly for business purposes when it is used to the extent of more than fifty percent for these purposes”.

The Tax Guide for Micro Businesses 2016/17 (issue 2) (SARS, 2017a: 19) points out that, notwithstanding the capital gains tax concession, it must be noted that a micro business includes fifty percent of the receipts on the disposal of an asset (excluding trading stock and financial instruments) in “taxable turnover”.

2.3.4 REGISTRATION AS A MICRO BUSINESS

In terms of paragraph 8(1) of the Sixth Schedule, registration as a “micro business” is at the election of the taxpayer. A person qualifying as a “micro business” may apply to SARS to register as a “micro business”, provided that the person was not previously deregistered as a “micro business”, either on a voluntary or compulsory basis. The Tax Guide for Micro Businesses 2016/17 (issue 2) (SARS, 2017a: 24) indicates that:

Two factors may necessitate a compulsory deregistration, namely –

- the qualifying turnover derived by the micro business from carrying on business activities during a year of assessment exceeds or is likely to exceed the R1 million threshold and the business cannot demonstrate that this will be a nominal and temporary event; or
- the person is disqualified in terms of paragraph 3 of the Sixth Schedule to the South African Income Tax Act.

The Tax Guide for Micro Businesses (issue 2) 2016/17 (SARS, 2017a: 26) explains further that “voluntary deregistration occurs when the owner of a registered micro business prefers to be taxed under the normal tax system and elects to deregister from the turnover tax system”.

2.3.5 OTHER TAX INCENTIVES AVAILABLE TO MICRO BUSINESSES

In terms of section 64F(1)(h) of the South African Income Tax Act, where a holder of a share in a company or close corporation, which is a registered micro business, receives a dividend from the registered micro business, the dividend will be exempt from dividends tax, provided that the total dividends paid by the company or closed corporation during the relevant year of assessment do not exceed R200 000.

The VAT 404 Guide for Vendors (SARS, 2017c: 14) has drawn attention to the fact that “a qualifying micro business that is registered for turnover tax may also choose to register for VAT provided that all the conditions for voluntary registration are met”. It appears that a “micro business” that voluntarily registers for VAT is registered as a Category D vendor and submits VAT returns twice a year. In terms of section 15(2)(b) of the Value-Added Tax Act, No. 89 of 1991, a natural person or partnership may account for VAT on the payments basis where the taxable supplies in a twelve-month period “ending at the end of any tax period has not exceeded R2.5m”. This would therefore apply to these persons qualifying as a “micro business”.

2.4 SMALL BUSINESS CORPORATIONS

The small business corporation regime was promulgated to encourage employment creation and promote skills development by introducing favourable depreciation rules for small businesses in the manufacturing industry (Manuel, 2001). Smulders and Oberholzer (2006: 3) report that section 12E was inserted into the South African Income Tax Act “to encourage small business to incorporate so that they can reap the benefits of a more formal approach to business”.

2.4.1 THE DEFINITION OF A SMALL BUSINESS CORPORATION

In terms of section 12E(4) of the South African Income Tax Act, certain requirements must be met before an entity can be classified as a small business corporation. Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 4) indicates that four requirements should be met when evaluating whether an entity qualifies as a small business corporation. The four requirements are:

- a legal entity requirement;
- a holder of shares requirement;
- a “gross income” limitation requirement; and
- a business activity requirement.

Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 4) also notes that the requirements must be met every year, as the position of the taxpayer may change from one year of assessment to the next.

2.4.1.1 LEGAL ENTITY REQUIREMENT

In terms of the legal entity requirement in section 12E(4)(a) of the South African Income Tax Act, any close corporation, co-operative, private company as defined in terms of section 1 of the Companies Act No 71, of 2008 (the South African Companies Act), or a personal liability company as defined in section 8(2)(c) of the South African Companies Act, may qualify as a small business corporation, provided that the other requirements are satisfied.

The Taxation Laws Amendment Act No 15, of 2016 expanded the definition of a “small business corporation” in section 12E(4)(a) of the South African Income Tax Act to include a personal liability company within the ambit of the legal entity requirement. The Explanatory Memorandum on the Taxation Laws Amendment Bill 17B of 2016 (National Treasury, 2016: 28) recognised that due to the implementation of the South African Companies Act in 2011, an anomaly arose where the definition of a “private company” as defined in the South African Companies Act specifically excluded a “personal liability company”. This amendment to section 12E(4)(a) came into effect with a retrospective application on 1 May 2011, the same date as the South African Companies Act came into effect.

2.4.1.2 HOLDER OF SHARES REQUIREMENT

In terms of section 12E(4)(a) of the South African Income Tax Act, the holders of shares or members of a close corporation or co-operative must be natural persons for the full year of assessment. Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 6) explains that where the shares or member's interest are held in a trust and the beneficiaries (who are natural persons) of the trust hold a vested right in the shares or member's interest for the full year of assessment, the entity may still qualify as a small business corporation. The indications are therefore that the beneficial ownership of the shares or member's interest is considered when evaluating the "holder of shares" requirement.

In terms of section 12E(4)(a)(ii) of the South African Income Tax Act, a natural person holding shares in a small business corporation is permitted to hold a limited class of shares or an interest in other entities. The permissible shareholding listed in section 12E(4)(a)(ii) is similar to the permissible shareholding provisions in terms of paragraph 4 read with paragraph 3 of the Sixth Schedule, as discussed in paragraph 2.3.1 above. Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 7) indicates that the prohibition of multiple shareholdings or arrangements is an anti-avoidance mechanism to prevent income being split between various entities.

2.4.1.3 GROSS INCOME REQUIREMENT

The "gross income" of the small business corporation may not exceed R20m for the "year of assessment" in terms of section 12E(4)(a)(i) of the South African Income Tax Act. Section 1 of the South African Income Tax Act, defines "gross income" as follows:

in relation to any year or period of assessment, means —

- (i) in the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident; or
- (ii) in the case of any person other than a resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such person from a source within the Republic,

during such year or period of assessment, excluding receipts or accruals of a capital nature.

In terms of section 1 of the South African Income Tax Act, “year of assessment” means:

Any year or other period in respect of which any tax or duty leviable under this Act is chargeable, and any reference in this Act to any year of assessment ending the last or the twenty-eighth or the twenty-ninth day of February shall, unless the context otherwise indicates, in the case of a company or a portfolio of a collective investment scheme in securities be construed as a reference to any financial year of that company or portfolio ending during the calendar year in question.

When the “year of assessment” is less than twelve months, the R20m “gross income” threshold in terms of section 12E(4)(a)(i) of the South African Income Tax Act must be apportioned for the number of months during the “year of assessment”. In terms of Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 9), however, if the “year of assessment” exceeds twelve months (for example, when the accounting year end is changed), the R20m threshold will not be increased.

2.4.1.4 BUSINESS ACTIVITY REQUIREMENT

In terms of section 12E(4)(a)(iii) of the South African Income Tax Act, if more than twenty percent of the total receipts and accruals (excluding receipts and accruals of a capital nature, but including capital gains) constitutes “investment income” and income from the rendering of a personal service, the entity does not qualify as a small business corporation. Therefore, the meaning of “capital gains”, “investment income” and “personal service” must be considered. Paragraph 3(a) of the Eighth Schedule of the South African Income Tax Act provides that the term “capital gain” denotes the difference between the proceeds and the base cost of the asset being disposed of.

In terms of section 12E(4)(c) of the South African Income Tax Act “investment income” is defined as:

- (i) any income in the form of dividends, foreign dividends, royalties, rental derived in respect of immovable property, annuities or income of a similar nature;
- (ii) any interest as contemplated in section 24J (other than any interest received by or accrued to any co-operative bank as contemplated in paragraph (a) (ii) (ff)), any

amount contemplated in section 24K and any other income which, by the laws of the Republic administered by the Commissioner, is subject to the same treatment as income from money lent; and

- (iii) any proceeds derived from investment or trading in financial instruments (including futures, options and other derivatives), marketable securities or immovable property.

Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 11) indicates that the letting of serviced accommodation on a short-term basis “will not be regarded as rental derived in respect of immovable property”.

Section 12E(4)(d) defines a “personal service” as:

“personal service” in relation to a company, co-operative or close corporation, means any service in the field of accounting, actuarial science, architecture, auctioneering, auditing, broadcasting, consulting, draftsmanship, education, engineering, financial service broking, health, information technology, journalism, law, management, real estate broking, research, sport, surveying, translation, valuation or veterinary science, if —

- (i) that service is performed personally by any person who holds an interest in that company, co-operative or close corporation; and
- (ii) that company, co-operative or close corporation does not throughout the year of assessment employ three or more full-time employees (other than any employee who is a holder of a share in the company or a member of the co-operative or close corporation, as the case may be, or who is a connected person in relation to a holder of a share in the company or a member), who are on a full-time basis engaged in the business of that company, co-operative or close corporation of rendering that service.

Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 13) states that “a personal service refers to a service rendered for which the income derived is mainly a reward for the personal efforts or skills of an individual”. Furthermore, according to the SARS (2016: 13), “any service in the field” refers to “every service in the specified field irrespective of whether it is of a professional nature”. It is submitted that both requirements in terms of section 12E(4)(d) of the South African Income Tax Act must be satisfied for the income derived from the entity to be classified as income from a “professional service”.

The requirements are:

- the service is provided by the beneficial holder of shares or a person with an interest in the entity; and
- the entity employs less than three full-time employees throughout the “year of assessment”.

According to Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 14):

An employee must –

- be engaged on a full-time basis in the qualifying entity’s business of performing the relevant service;
- not be a holder of shares in or a member of the qualifying entity; and
- not be a connected person in relation to a holder of shares in or a member of the qualifying entity.

Furthermore, Interpretation Note 9: Small Business Corporations (issue 6) (SARS, 2016: 14) makes clear that the “personal service” requirements are there to “encourage the creation of full-time employment”.

In terms of section 12E(4)(a)(iv) of the South African Income Tax Act a “personal service provider” is excluded from being a Small Business Corporation. A “personal service provider” is defined in terms of section 1 of the Fourth Schedule to the South African Income Tax Act, as discussed in section 2.3.1 above. It appears that the requirements of a “personal service provider” are similar to that of a “personal service”. However, in addition, a person will be regarded as a “personal service provider”:

- where more than eighty percent of the income of the entity is received from one client (or an associated institution in relation to the client) during the year of assessment; and
- the services are mainly performed at the premises of the client, subjected to the control and supervision of the client in relation to the manner in which the services are performed.

Therefore, a company would need to consider if more than twenty percent of income received or accrued (excluding that of a capital nature) plus capital gains, is received or accrued from investment income or a “personal service”, as well as whether the company may be considered a “personal service provider”.

2.4.2 SMALL BUSINESS CORPORATION INCOME TAX INCENTIVES

Section 12E(1) of the South African Income Tax Act provides that plant or machinery (the asset) used in the process of manufacture or a similar process qualifies for a deduction of 100% of the cost of the asset, provided that:

- the asset is owned by the taxpayer or acquired in terms of an “instalment credit agreement”;
- the asset is used in the taxpayer's trade; and
- brought into use for the first time during the “year of assessment”.

In terms of section 12E(1A) of the South African Income Tax Act read with section 11(e) of the South African Income Tax Act, non-manufacturing assets are written-off over a period of three years:

- fifty percent of the cost in the year the asset is brought into use for the first time;
- thirty percent in the next year and
- twenty percent in the final year.

Section 12E(1A) provides the taxpayer with an election to either depreciate the asset in terms of section 12E(1A) or section 11(e). Section 11(e) of the South African Income Tax Act, read with Interpretation Note 47 (issue 3) - Wear and Tear Depreciation Allowance (SARS, 2012: 14) provides for the write-off of 100% of the cost of an asset (referred to as a small item) in the year of assessment the small item is brought into use. A small item is an asset with a Value-Added Tax exclusive cost of R7 000 or less. Where the cost of a non-manufacturing asset is R7 000 or less, a taxpayer is likely to elect the provisions of section 11(e) read with Interpretation Note 47, as this provides for the write-off of the full cost in the year of assessment

the asset is brought into use, in contrast to the three-year write off period provided for in section 12E(1A).

A progressive tax rate applies to Small Business Corporations. Table 2.2 illustrates the tax rates applicable for the year of assessment ending on any date between 1 April 2017 and 28 February 2018.

Table 2.2: Small Business Corporation tax tables: 1 April 2017 to 31 March 2018

| Taxable Income (R) | Rate of Tax (R) |
|--------------------|--|
| 0 – 75 750 | 0% |
| 75 751 – 365 000 | 7% of taxable income above 75 750 |
| 365 001 – 550 000 | 20 248 + 21% of taxable income above 365 000 |
| 550 001 and above | 59 098 + 28% of taxable income above 550 000 |

Source: SARS (2017d: online)

2.5 SMALL BUSINESS CAPITAL GAINS TAX RELIEF

Paragraph 57 of the Eighth Schedule provides the legislative framework for the disposal of “small business” assets. The Comprehensive Guide to Capital Gains Tax (issue 5) (SARS, 2015: 444) observes that “the purpose of this paragraph is to provide relief to small business persons who have invested their resources in their businesses”.

2.5.1 THE DEFINITION OF A SMALL BUSINESS

In terms of paragraph 57 of the Eighth Schedule a “small business” is defined as “a business, where the market value of all the business assets or interest in those assets at the date of disposal does not exceed R10m”. The Comprehensive Guide to Capital Gains Tax (issue 5) (SARS, 2015: 445) points out that:

In determining whether a business qualifies, the market value of all the assets, regardless of their nature, must be taken into account. Furthermore, the liabilities of the business must be ignored for this purpose. In the case of a business operated by a partnership or company, the threshold of R10m relates to the assets of the partnership or company as a whole, and

not to the fractional interest of each partner or shareholder in the underlying assets of the business.

2.5.2 THE REQUIREMENTS IN TERMS OF PARAGRAPH 57 OF THE EIGHTH SCHEDULE

Paragraph 57(3) provides for an exclusion of R1.8 million in respect of the capital gain or loss on the disposal of small business assets. In terms of paragraph 57(2) the aggregate capital gain or loss that is subject to the R1.8m exclusion must be in respect of:

- A natural person disposing of
 - their active business assets as a small business sole-proprietor;
 - their interest in the active business assets of a partnership which qualifies as a small business; or
 - their interest in the active business assets of a company which qualifies as a small business, where at least a ten percent interest is held by the natural person.
- The active business asset must have been held for a continuous period of at least five years prior to the disposal of that asset, and the natural person must have been actively involved in the operations of the small business.
- The natural person should be 55 years old or have disposed of the active business asset due to ill health, disability, retirement or death.

The question is what constitutes an “active business asset”? In terms of paragraph 57(2) of the Eighth Schedule an “active business asset” means:

- (a) an asset which constitutes immovable property, to the extent that it is used for business purposes; or
 - (b) an asset (other than immovable property) used or held wholly and exclusively for business purposes,
- but excludes —
- (i) a financial instrument; and
 - (ii) an asset held in the course of carrying on a business mainly to derive any income in the form of an annuity, rental income, a foreign exchange gain or royalty or any income of a similar nature.

The Comprehensive Guide to Capital Gains Tax (issue 5) (SARS, 2015: 444) points out that where immovable property is not wholly used for business purposes, a reasonable apportionment will need to be made between business and non-business use and that assets used to generate passive income will not constitute an active business asset.

In terms of paragraph 57(4) of the Eighth Schedule, the full amount of the capital gain should be realised within twenty-four months from the date of the first disposal. Paragraph 57(5) of the Eighth Schedule indicates that a natural person operating more than one small business may include all qualifying disposals for every such small business in determining the capital gain to be disregarded in terms of paragraph 57(3). This provision is subject to the capital gains being realised within 24 months of the first disposal and the provisions of paragraph 57(6). In terms of paragraph 57(6) the R1.8m exclusion will not apply in a situation where a natural person has multiple businesses, and the total market value of all the assets in the businesses exceeds R10m. The Comprehensive Guide to Capital Gains Tax (issue 5) (SARS, 2015: 446) reveals that “in determining whether the R10 million threshold has been exceeded the interests in all businesses and not just small businesses must be included. Likewise, all assets used in a business must be included, even if they produce passive income”.

In terms of paragraph 57(3) read with paragraph 57(2) of the Eighth Schedule, a natural person may disregard up to a maximum of R1.8m of their aggregate capital gain or aggregate capital loss during that natural person’s lifetime. On this basis, it may be inferred that the R1.8 exclusion is a cumulative exclusion.

2.6 EXPENDITURE INCURRED IN EXCHANGE FOR THE ISSUE OF VENTURE CAPITAL COMPANY SHARES

The External Guide: Venture Capital Companies (revision 7) (SARS, n.d.: 3) states that:

One of the main challenges to the growth of small and medium-sized businesses and junior mining exploration is access to equity finance. To assist these sectors in terms of equity finance, the government has implemented a tax incentive for investors in these enterprises through a venture capital company (VCC) regime. VCCs are intended to be a marketing vehicle that will attract retail investors.

In terms of section 12J(2) of the South African Income Tax Act:

Subject to subsections (3), (3A) and (4), there must be allowed as a deduction from the income of a taxpayer expenditure actually incurred by that taxpayer in acquiring any venture capital share issued to that taxpayer by a venture capital company.

Section 12J(4) of the South African Income Tax Act provides that “a claim for a deduction in terms of subsection (2) must be supported by a certificate issued by the venture capital company stating the amounts invested in that company and that the Commissioner approved that company as contemplated in subsection (5)”.

On this basis, taxpayers in possession of an investor certificate may claim a 100% tax deduction in respect of their investment in a venture capital company.

Further discussion is required to establish what is meant by:

- a taxpayer;
- actually incurred;
- venture capital share; and
- venture capital company.

The External Guide: Venture Capital Companies (revision 7) (SARS, n.d.: 7) explains that “*any* taxpayer qualifies to invest in an approved venture capital company” (own emphasis). The term “actually incurred” is not defined in the South African Income Tax Act. Corbett JA, in *Edgars Stores Ltd v CIR*, 1988(3) SA 876 (A), 50 SATC 81, held (at 90): “... only expenditure (otherwise qualifying for deduction) in respect of which the taxpayer has incurred *an unconditional legal obligation* during the year of assessment in question may be deducted ...” (own emphasis).

In terms of section 12J(1) of the South African Income Tax Act, a “venture capital share”:

means an equity share held by a taxpayer in a venture capital company which is issued to that taxpayer by a venture capital company, and does not include any share which —

(a)

- (b) would have constituted a hybrid equity instrument, as defined in section 8E (1), but for the three-year period requirement contemplated in paragraph (a) of the definition of “hybrid equity instrument” in that section; or
- (c) constitutes a third-party backed share as defined in section 8EA (1).

Therefore, hybrid equity instruments in terms of section 8E(1) of the South African Income Tax Act and third-party backed shares in terms of 8EA(1) of the South African Income Tax Act will not constitute a venture capital share for the purposes of section 12J of the South African Income Tax Act. An “equity share” is defined in terms of section 1 of the South African Income Tax Act as “any share in a company, excluding any share that, neither as respects dividends nor as respects returns of capital, carries any right to participate beyond a specified amount in a distribution”.

Section 12J(1) of the South African Income Tax Act describes a “venture capital company” as “a company that has been approved by the Commissioner in terms of subsection (5) and in respect of which such approval has not been withdrawn in terms of subsection (6) or (6A)”. The External Guide: Venture Capital Companies (revision 7) (SARS, n.d.: 8) states that, in terms of section 12J(5) of the South African Income Tax Act, the following requirements must be met for each “year of assessment” to qualify for approved venture capital company status:

- the company must be a resident;
- the sole object of the company must be the management of investments in qualifying companies (i.e. investees);
- the company’s tax affairs must be in order;
- the company must be licensed in terms of section 7 of the Financial Advisory and Intermediary Services Act, No. 37 of 2002.

Approval as a venture capital company may be withdrawn in terms of section 12J(6) where the Commissioner is satisfied that, during the year of assessment, the venture capital company failed to comply with the provisions of section 12J(5). The approval status is withdrawn after due notice has been provided to the venture capital company if corrective steps were not implemented within the period provided for in the notice. The approval status will be withdrawn from the commencement of the “year of assessment” in which the requirements in terms of section 12J(5) were not met.

In relation to section 12J(6A) of the Act, the External Guide: Venture Capital Companies (revision 7) (SARS, n.d.: 9) states that:

The company must satisfy the following requirements by the end of each year of assessment after the expiry of 36 months from the first date of issue of venture capital shares:

- A minimum of 80% of the expenditure incurred by the VCC to acquire assets must be for qualifying shares, and each investee company must, immediately after the issuing of the qualifying shares, hold assets with a book value not exceeding:
 - R500m in any junior mining company; or
 - R50m in any other qualifying company.
- The expenditure incurred by the VCC to acquire qualifying shares in any one qualifying company must not exceed 20% of any amounts received in respect of the issue of venture capital shares.

Section 12J(6A) of the South African Income Tax Act provides that:

... the Commissioner must after due notice to the company withdraw that approval with effect from the date of approval by the Commissioner of that company as a venture capital company if corrective steps acceptable to the Commissioner are not taken by the company within a period stated in the notice.

In terms of section 12J(3A) a taxpayer will not be entitled to the deduction provided for in section 12J(2) if at the end of any year of assessment the taxpayer is a connected person in relation to the venture capital company. This prohibition is only effective after thirty-six months from the date of the first issue of venture capital shares to the taxpayer.

The External Guide: Venture Capital Companies (revision 7) (SARS, n.d.: 7) points out that:

If corrective steps acceptable to the Commissioner are not taken by the company, the Commissioner will withdraw the approval of that company and an amount equal to 125% of the aggregate amount contributed by the qualifying investor in exchange for VCC certificates will be included in the VCC income in the year of assessment in which such approval has been withdrawn.

Where a taxpayer disposes of the venture capital shares within five years, the amount allowed as a deduction in terms of section 12J(2) will be recouped in terms of section 12J(9), read with section 8(4) of the South African Income Tax Act.

The External Guide: Venture Capital Companies (revision 7) (SARS, n.d.: 8) points out that “there are no special tax rules for approved venture capital companies. The standard tax rules apply”

2.7 CONCLUSION

This chapter has identified what constitutes a small business for South African Income Tax purposes, outlined the incentives available to small businesses in South Africa and the deductions available to investors in small business. It has been shown from this review that the South African tax legislation provides three tax incentives for small business in South Africa, namely:

- turnover tax for micro businesses;
- accelerated allowances and reduced tax rates for small business corporations; and
- capital gains tax relief on the disposal of small business assets.

Investors in small businesses obtain a tax deduction for their investment, provided that the investment is made in an approved venture capital company.

The turnover tax regime provides micro businesses with a simplified tax system known as “turnover tax”. The “turnover tax” liability replaces the normal income tax, VAT, provisional tax and capital gains tax obligations. Where a micro business receives any income that does not constitute “qualifying turnover”, however, the normal tax rules will apply. A micro business may voluntarily register for VAT if the requirements for voluntary registration are satisfied.

Section 12E of the South African Income Tax Act provides manufacturers qualifying as a “small business corporation” with tax relief in the form of accelerated capital allowances and a reduced rate of tax, based on the progressive level of taxable income. A small business

corporation may claim 100% of the cost of manufacturing assets brought into use for the first time, in the process of manufacture. Favourable allowances exist for non-manufacturing assets, which are written off over three years.

It is submitted that the incentives may assist small businesses, but the requirements to be classified as a “micro business” or “small business corporation” are onerous and very narrow. It appears that there is no specific incentive for a start-up company, but it may be inferred that the thresholds (R1m for “turnover tax” and R20m for a “small business corporation”) will provide a start-up company access to the “turnover tax” and “small business corporation” incentives.

The capital gains tax relief in terms of paragraph 57 of the Eighth Schedule provides a lifetime capital gain exclusion of R1.8m for active small business assets.

Section 12J of the South African Income Tax Act was introduced to provide small business with access to equity finance. The investor must be in the possession of an investor certificate issued by an approved venture capital company. The approved venture capital company is only allowed to invest in an investee as prescribed by section 12J(5) of the South African Income Tax Act. Section 12J does not provide a deduction for a direct equity investment in a small business.

In the following chapter, the definition of a small business and the tax incentives available to the small businesses and the investors in the small businesses in Australia, New Zealand, Singapore and Ireland will be discussed.

CHAPTER 3: SMALL BUSINESS TAX RELIEF MEASURES IN SELECTED INTERNATIONAL JURISDICTIONS

3.1 INTRODUCTION

In addressing one of the sub-goals of the research, this chapter identifies the existing tax relief measures available to small, medium and micro-sized businesses, and investors in these businesses, in Australia, New Zealand, Singapore and Ireland.

Du Toit (2012: 1) concluded in her study that “the tax incentives in South Africa are on par with those of the developed countries such as Australia and Canada. Australia was therefore selected for the present research. The World Bank Group (2016: 1) ranked Singapore number one and New Zealand number two, based on the ease of doing business. This ranking was based on the “regulations and regulatory processes” in the respective countries. The Irish Tax Institute (2014: online) explains that Ireland introduced amendments to the Employment Investment Incentive Scheme and the Seed Capital Scheme, in an attempt to attract investments in small business. The Irish Tax Institute (2015: online) points out that “a number of measures aimed at encouraging entrepreneurship and supporting small business owners” were introduced in the 2016 Budget. On the basis of the favourable tax provisions for small businesses, these international jurisdictions were selected for the purpose this research.

In this chapter, definitions that are provided for a small, medium and micro-sized enterprise for income tax purposes, as well as the tax incentives available for these small businesses and investors in small businesses in the selected jurisdictions are identified and discussed.

3.2 AUSTRALIA

The Australian Treasury (2017: 1) asserts that ninety-seven percent of all businesses in Australia comprises of small businesses. Furthermore, the Australian Treasury (2017: 3) points out that 44.8% of private sector employment (excluding financial, insurance and public sectors) is attributable to small businesses in Australia. Small businesses contribute 35.6% of total industry value (excluding financial, insurance and public sectors) to the Australian economy.

3.2.1 THE DEFINITION OF A SMALL BUSINESS IN AUSTRALIA

The Australian Taxation Office (2017a: online) refers to a small business as a “small business entity” for tax purposes. A “small business entity” is defined in terms of section 328(110) of the Australian Income Tax Assessment Act, No 38 of 1997 (the Australian Income Tax Act), as:

- a sole trader, partnership, company or trust;
- that operates a business for the “income year” (or part thereof); and
- the “aggregated turnover” for the previous year, while carrying on a “business” is less than AUD10m or the “aggregated turnover” is likely to be less than AUD10m in the current “income year”.

The following terms require further discussion:

- a “business”;
- “income year”; and
- “aggregated turnover”.

Section 995(1) of the Australian Income Tax Act defines a “business” as “any profession, trade, employment, vocation or calling, but does not include occupation as an employee”. The tax liability is calculated for the “income year”. In terms of section 995(1) read with sections 4(10)(2) and 9(5)(2) of the Australian Income Tax Act an “income year” is equal to the “financial year”. A “financial year” is the twelve-month period beginning 1 July each year. For a company, the “income year” will be equal to the previous “financial year”.

Section 328(115) of the Australian Income Tax Act states that the “aggregated turnover” represents the “annual turnover” of the taxpayer plus the “annual turnover” of any entity “connected” to, or an “affiliate” of, the taxpayer. In terms of section 328(120) of the Australian Income Tax Act, the “annual turnover” refers to “ordinary income derived” in the ordinary course of running a business for the “income year”. The annual turnover excludes amounts “derived” from transactions concluded with relevant entities “connected” to the taxpayer or “affiliates” of the taxpayer, General Sales Tax and “ordinary income derived” from the sale of

retail fuel. Section 328(120)(5) of the Australian Income Tax Act provides that where an entity does not carry on a business for the full “income year” a “reasonable estimate” must be made to calculate the “annual turnover” for a twelve month period.

Section 328(125) of the Australian Income Tax Act provides that a taxpayer is “connected” to another entity where one entity is controlled by another entity, or both entities are controlled by the same party. “Control” is defined as the situation where an entity, its affiliates or an entity and its affiliates has an equity interest that provides at least forty percent of the voting power in the entity or provides the right to at least forty percent of the income or capital the company distributes.

An “affiliate” is defined in terms of section 328(130) of the Australian Income Tax Act. An individual or company will be an affiliate of the taxpayer, where the individual or company acts under the direction or wishes of the taxpayer or “in concert” with the taxpayer in respect of their business affairs. The Australian Taxation Office (2017b: online) has indicated that “in concert” refers to a relationship of dependence on the taxpayer. Section 328(128) of the Australian Income Tax Act indicates that an individual or company will not automatically be an “affiliate” of the taxpayer due to the nature of their business relationship.

The “aggregated turnover” for the “income year” is calculated in terms of sections 328(115) and 328(120) of the Australian Income Tax Act. There are three methods to determine the “aggregated turnover” when calculating the “small business entity” threshold:

- the “aggregated turnover” for the previous “income year”;
- the estimated current year “aggregated turnover” as at the beginning of the current year; or
- the actual “aggregated turnover” as at the end of the current “income year”.

In calculating the “aggregated turnover” for the current year, section 328(110)(2) of the Australian Income Tax Act provides that the general rule is that the “aggregated turnover” is calculated on the first day of the current year or at the commencement date of a business, in the year a business commences. Where the “aggregated turnover” for the previous “income year” is selected, the taxpayer will be a “small business entity” in the current “income year” if

the “aggregated turnover” is AUD10m or less in the previous “income year”. If a taxpayer elects to use the current year estimated “aggregated turnover”, the election is only available if the “aggregated turnover” was less than AUD10m in one of the previous two “income years”. Where the taxpayer elects to use the actual “aggregated turnover”, the actual “aggregated turnover” must be less than AUD10m for the “income year”. The same method should be used for “connected” or “affiliate” entities and record must be kept of how the “aggregated turnover” was calculated.

In terms of section 328(110)(5) of the Australian Income Tax Act, if a “small business entity” as defined is wound up in an “income year” and a “business” was previously carried on, the “business” will still qualify as a “small business entity” in the year of winding up.

A taxpayer will not qualify as a “small business entity” in the current year, in terms of section 328(110)(3) of the Australian Income Tax Act, where a business was carried on in each of the two preceding “income years” and the “aggregated turnover” exceeded AUD10m in each of the preceding two “income years”. Section 328(110)(6) of the Australian Income Tax Act states that where a partnership qualifies as a “small business entity” the individual partners do not qualify as a “small business entity”.

3.2.2 SMALL BUSINESS ENTITY INCOME TAX INCENTIVES

Australia provides a wide spectrum of tax incentives, including the deduction of start-up expenses, simplified depreciation and trading stock rules, a small business income tax offset, the immediate deduction of pre-paid expenses, a reduced corporate tax rate, fringe benefit and capital gains tax concessions and a number of goods and services tax concessions.

3.2.2.1 IMMEDIATE DEDUCTIBILITY FOR START-UP EXPENSES

In terms of section 40(880)(2A) of the Australian Income Tax Act, capital expenditure incurred for a business that is proposed to be carried on, is fully deductible in the “income year” the expenditure is incurred, provided that the expenditure relates to the start-up cost of a “small business entity”. Section 40(880)(2A) of the Australian Income Tax Act states that the type of start-up cost that will be deductible must relate to professional advice and services in respect

of the structure or the operations of the proposed business. Payments to Australian government agencies for fees, charges and taxes relating to establishing the business or the operating structure will qualify as a deduction in terms of section 40(880)(2A) of the Australian Income Tax Act.

3.2.2.2 SIMPLIFIED DEPRECIATION RULES

Section 328(175) of the Australian Income Tax Act provides that a taxpayer may elect to apply the simplified depreciation rules to “depreciating assets” if the following requirements are satisfied:

- the taxpayer is a “small business entity” as defined; and
- the asset is used or “installed ready for use” in the “income year” or previous “income year” for a “taxable purpose”.

The term “installed ready for use” is defined in section 995(1) of the Australian Income Tax Act and means “installed, ready for use and held in reserve”. “Depreciating assets” in terms of section 40(30)(1) of the Australian Income Tax Act refers to an asset that reduces in value over time with a finite useful life, but excludes land, trading stock and intangible assets that are not specifically depreciable in terms of the Australian Income Tax Act.

In terms of section 328(180) of the Australian Income Tax Act, a taxpayer may elect that assets acquired between 15 May 2015 and 30 June 2018 with a cost of less than AUD20 000 will be deductible in full in the “income year” the asset is brought into use or “installed ready for use”. It appears that the asset may be new or second hand.

Section 328(185) of the Australian Income Tax Act states that a “small business entity” may elect to depreciate assets with a cost of AU\$20 000 or more by allocating the individual assets to a “general small business pool” and depreciate the pool as a single asset. Section 328(190) states that in the year the assets are brought into use or are “installed ready for use”, the depreciation rate is fifteen percent, and every year thereafter the depreciation rate is thirty percent. A “small business entity” may deduct the full pool balance as calculated in terms of section 328(210), where the balance is below AUD20 000.

3.2.2.3 SIMPLIFIED TRADING STOCK RULES

Section 328(285) of the Australian Income Tax Act states that if a “small business entity” elects the provisions of the section, it will qualify for the simplified trading stock rules where the difference between the value of opening and closing trading stock during for an “income year” does not exceed AUD5 000. The Australian Taxation Office (2017c: online) points out that the difference of AUD5 000 may either refer to an increase or a decrease in the trading stock value during the “income year”. In terms of section 328(295) the “small business entity” does not account for the change in the value of trading stock for the “income year”, and therefore the closing stock value at the end of the year will be equal to the opening stock value at the start of the year. The Australian Taxation Office (2017c: online) explains that when a “small business entity” elects the simplified trading stock rules, there is no requirement to conduct a stock take at the end of the “income year”.

3.2.2.4 SMALL BUSINESS INCOME TAX OFFSET

For the purposes of the small business income tax offset, section 328(157) of the Australian Income Tax Act defines a “small business entity” as an entity with an “aggregated turnover” of less than AUD5m. Section 328(350) of the Australian Income Tax Act states that an individual that qualifies as a “small business entity” as defined (a sole trader) or an individual that includes any of the following in assessable income: a share of the “net small business income” from an unincorporated entity, an amount from a partnership or an amount due to being a beneficiary of a trust, may be entitled to the small business income tax offset.

In terms of section 328(360) of the Australian Income Tax Act, the offset is calculated as the greater of:

- $8\% \times \{(total\ net\ small\ business\ income\ for\ the\ income\ year / taxable\ income\ for\ the\ income\ year) \times the\ basic\ income\ tax\ liability\ for\ the\ income\ year\}$; or
- AUD1 000.

Therefore, the offset is the greater of the tax on the individual’s small business income portion or AUD1 000. The “net small business income” in terms of section 328(360) of the Australian Income Tax Act refers to the sole trader’s “net small business income” or the portion of the

“net small business income” received from a partnership, trust or an unincorporated entity. The “net small business income” may not exceed the taxable income for the “income year”. In terms of section 328(365) the “net small business income” refers to the business income after taking into account the allowable deductions but excluding the net capital gain and personal service income not generated from a personal service business.

3.2.2.5 DEDUCTION FOR PREPAID EXPENDITURE

In terms of section 82KZM of the Income Tax Assessment Act No 27, of 1936 a “small business entity” may elect to deduct prepaid expenditure in the “income year” the expense is incurred, even though not all the goods or services are delivered in that “income year”. The expenditure refers to both business and non-business expenses incurred by the “small business entity”. An expense is regarded as prepaid expenditure where the “eligible service period” for the expenditure exceeds twelve months, or the eligible service period is a maximum of twelve months, but the period ends after the end of the “income year” in which the expenditure is incurred. The “eligible service period” is defined as the lesser of ten years or the period over which the services will be rendered, or goods provided. For a “small business entity” to qualify for the immediate deduction, the “eligible services period” refers to a maximum of twelve months and the “eligible service period” ends not later than the last day of the “income year” following the “income year” in which the expense is incurred. If the “eligible service period” exceeds 12 months, the expense will be deducted over the “eligible service period”.

Section 82 KZL of the Income Tax Assessment Act No 27, of 1936 states that the following expenditure is regarded as “excluded expenditure” and would therefore not be apportioned over the eligible service period, but will be deducted in full in the year incurred, expenditure:

- with a cost of less than AUD1 000;
- imposed by legislation;
- in terms of a service contract;
- to the extent that it is capital in nature and not deductible in terms of the Research and Development provisions;
- private and domestic expenditure; or
- by a general insurance company relating to insurance premium income or reinsurance.

3.2.3 FRINGE BENEFIT TAX CONCESSIONS

Employers of small business entities will be granted certain fringe benefit concessions. In terms of section 66 of the Fringe Benefit Tax Assessment Act No. 39 of 1986 (the Fringe Benefit Tax Act) an employer is liable for tax on fringe benefits granted to employees. It is submitted that the Fringe Benefit Tax concessions are granted to a “small business entity” to relieve the employer of the Fringe Benefit Tax obligation.

3.2.3.1 CAR PARKING EXEMPTION

In terms of section 58GA the Fringe Benefit Tax Act, where an employer provides an employee with a car parking facility, the employer will be exempt from paying “fringe benefit tax” on the car parking benefit, if all the following requirements are satisfied:

- “the car is not parked at a commercial parking station”;
- the employer is not a public company, a subsidiary of a public company or a government body; and
- the employer is a “small business entity” as defined for the “income year” preceding the fringe benefit tax year or the total income of the employer does not exceed AUD10m in the “income year” preceding the fringe benefit tax year.

3.2.3.2 WORK-RELATED DEVICE EXEMPTION

Section 58X of the Fringe Benefit Tax Assessment Act states that from 1 April 2016 a “small business entity” is exempt from levying fringe benefit tax on a “portable electronic device”. The requirement is that the employer has been a “small business entity” for an “income year” that commences or ends within the fringe benefit tax year and the “portable electronic device” is primarily used for employment purposes.

The Australian Taxation Office (2017d: online) explains that a “portable electronic device”:

- is easily portable and designed for use away from an office environment
- is small and light

- can operate without an external power supply
- is designed as a complete unit.

Furthermore, the Australian Taxation Office (2017d: online) indicates that the following qualifies as a “portable electronic device”:

- mobile phones
- calculators
- personal digital assistants (PDAs)
- laptop computers
- portable printers
- portable global positioning system (GPS) navigation receivers.

3.2.4 CAPITAL GAINS TAX CONCESSIONS

The basic conditions in terms of section 152(10) of the Australian Income Tax Act must be satisfied before the small business capital gains tax concessions could be considered. The basic conditions are as follows:

- the taxpayer must be a small business entity for the “income year” for capital gains tax purposes;
- the taxpayer satisfies the maximum net asset value test;
- the taxpayer’s capital gains tax asset is used in a business that is connected to or is an affiliate to the taxpayer, provided that the taxpayer does not carry on a business (except as a partner in a partnership); or
- the taxpayer is a partner in a partnership that qualifies as a “small business entity” and the capital gains tax asset is either the partner’s interest in a partnership asset or an asset used in the partnership but owned by the individual partner; and
- the asset is an “active asset”.

In terms of section 152(10)(1AA) a “Capital Gains Tax small business entity” for an “income year” is defined as a “small business entity” with an “aggregated turnover” that does not exceed AUD2m. This is in contrast to the “aggregated turnover” threshold of AUD10m of a “small business entity” applicable to income tax concessions.

Section 152(15) of the Australian Income Tax Act states that the maximum net asset value test is satisfied where the value of the net assets owned by the taxpayer, entities connected to the taxpayer or affiliates in relation to the taxpayer does not exceed AUD6m. The net value of the capital gains tax assets is calculated in terms of section 152(16) as the market value of the assets, less any outstanding liabilities in relation to the asset.

In terms of section 152(35) the “active asset” test is satisfied where the asset is owned and:

- used or is ready for use in the business conducted by the taxpayer;
- is an intangible asset which forms an integral part of the business;
- where the asset is owned for more than fifteen years, it is used for seven and a half years or more; or
- where the asset is owned for less than fifteen years, it is used for at least half the number of years it was owned.

3.2.4.1 CAPITAL GAINS TAX 15-YEAR ASSET EXEMPTION

In terms of sections 152(105) and 152(110) of the Australian Income Tax Act, the exemption is available to individuals, companies and trusts. The exemption allows the taxpayer to disregard the capital gain on the disposal of an asset, if the additional requirements identified below are satisfied.

Section 152(105) sets out the additional requirements for an individual:

- the asset was owned for a continuous period of fifteen years prior to disposal;
- the disposal is due to the taxpayer attaining the age of fifty-five and the disposal is in connection with their retirement or the individual is permanently incapacitated; and
- where the asset being disposed of is a share in a company or an interest in a trust, it is required that the company or trust must have had a “significant individual” for fifteen years or more.

Section 152(110) sets out the additional requirements for a company or trust:

- the asset was owned by the company or trust for a continuous period of fifteen years prior to disposal;
- the company or trust must have had a “significant individual” for fifteen years or more; and
- a “significant individual” to the company or trust attained the age of fifty-five and the disposal is in connection with their retirement or the individual is permanently incapacitated.

In terms of section 152(55) of the Australian Income Tax Act, a “significant individual” is defined as an individual with a direct or indirect interest in a company or trust of at least twenty percent.

3.2.4.2 CAPITAL GAINS TAX 50% ACTIVE ASSET REDUCTION

In terms of section 152(105) read with section 152(220) of the Australian Income Tax Act, a taxpayer may elect to reduce the capital gain by fifty percent if the basic conditions in terms of section 152(10) are satisfied. In terms of section 152(110), the reduced capital gain may be subject to the small business retirement exemption and the small business rollover relief. Section 152(215) states that where the fifteen-year asset exemption applies, the fifty percent active asset reduction will not apply, as the full capital gain was disregarded in terms of the fifteen-year asset exemption.

3.2.4.3 CAPITAL GAINS TAX RETIREMENT EXEMPTION

In terms of section 152(305) of the Australian Income Tax Act, an individual may elect to disregard the capital gain on the disposal of an asset up to a lifetime limit of AUD500 000 in terms of section 152(320) of the Australian Income Tax Act, were the following conditions are satisfied:

- the basic conditions are complied with in terms of section 152(10);

- the individual is below the age of fifty-five before the choice is made and the amount the individual would like to exempt is contributed towards an approved superannuation fund or retirement savings account; and
- the contribution is made at the time of the relevant capital gains tax event or when the proceeds are received.

In terms of section 152(300) the individual may elect the application of the fifty percent active asset reduction before the application of the retirement exemption. The remainder of the capital gain may be subject to the small-business rollover if the requirements as discussed in paragraph 3.2.4.4 below, are satisfied. In terms of section 152(330), where the fifteen-year capital gains tax exemption applied, the capital gains tax retirement exemption does not apply, as the capital gain was disregarded.

3.2.4.4 CAPITAL GAINS TAX ROLLOVER

In terms of section 152(410), read with section 152(145) of the Australian Income Tax Act, a taxpayer may elect to defer the capital gain where the basic conditions in terms of 152(10) are satisfied and a replacement asset is purchased. Section 152(400) states that the taxpayer may elect not to apply the fifty percent active asset reduction. In terms of section 152(430) where the fifteen-year exemption applied, the capital gains tax roll over does not apply, as the capital gain was disregarded.

3.2.4.5 RESTRUCTURE OF A SMALL BUSINESSES

Section 328(420), read with sections 328(425), 328(430), 328(445) of the Australian Income Tax Act, states that from 1 July 2016 an Australian resident “small business entity” may restructure the ownership of the assets without creating a tax liability, provided that the “ultimate economic ownership” of the assets does not change. This concession is available where a “small business entity” (or an affiliate, or a connected entity or a partner in a small business entity partnership) transfers an “active business asset” from one “small business entity” to another. The “small business entity” may elect this provision when the transfer relates to a “genuine restructure” of an ongoing business. In terms of section 328(435) of the Australian Income Tax Act, a restructure will be considered a “genuine restructure” where

three years after the transaction there is no change in the economic ownership of the assets, provided that the assets continue to be used as “active business assets” and the assets are not significantly used for private purposes.

3.2.5 CORPORATE TAX RATE

The Australian Taxation Office (2017e: online) points out the corporate tax rate for a “small business entity” for the 2016/2017 “income year” is 27.5%, while the corporate tax rate for other companies is 30%.

3.2.6 GOODS AND SERVICES TAX CONCESSIONS

There are a number of Goods and Services Tax concessions as described below. In terms of section 23(15) of the Goods and Services Tax Act, No. 55 of 1999 (the Australian GST Act), read with Regulation 23.15.01 (Minister of Finance, 1999: online) the Goods and Service Tax registration threshold is AUD 75 000.

3.2.6.1 ACCOUNTING FOR GOODS AND SERVICES TAX ON THE CASH BASIS

In terms of section 29(40) of the Australian GST Act, a taxpayer may elect to account for Goods and Services Tax on a cash basis. The Australian Taxation Office (2017f: online) points out that by electing the cash basis, the taxpayer will only account for the Goods and Services Tax once payment is received and the taxpayer will only be entitled to claim the input tax credits once payment has been made. A taxpayer may apply to the Commissioner to account for the Goods and Services Tax in terms of section 29(45) of the Australian GST Act if the following requirements in terms of section 29(40) of the Australian GST Act are satisfied:

- the taxpayer is a “small business entity” as defined for the “income year” in which the election is made;
- the taxpayer is not carrying on a business and the enterprise’s Goods and Services Tax turnover is AUD 2m or less (for example, a not-for-profit organisation);
- income tax is accounted for on the cash basis; or

- the taxpayer carries on an enterprise that the Commissioner agrees may register for Goods and Services tax on the cash basis.

3.2.6.2 ANNUAL APPORTIONMENT OF GOODS AND SERVICES TAX CREDIT

In terms of section 131(5) of the Australian GST Act, a taxpayer may elect to claim the full input credit on purchases relating to both business and private use. After the end of the “income year”, a once-off apportionment will be made to reverse the input credits claimed relating to private use of goods or services. The Australian Taxation Office (2017g: online) refers to this adjustment as the “annual private apportionment adjustment”. A taxpayer may elect the “annual private apportionment adjustment” in terms of section 131(5) of the Australian GST Act, if the following requirements are satisfied:

- the taxpayer is a “small business entity” as defined for the “income year” in which the election is made; or
- the taxpayer is not carrying on a business and the enterprise’s Goods and Services Tax turnover is AUD 2m or less (for example, a not-for-profit organisation); and
- no election was made to pay Goods and Services Tax by instalments;
- no election was made to report Goods and Services Tax an annual basis.

The Australian Taxation Office (2017f: online) points out that the taxpayer is not required to notify the Commissioner of the election but must keep a record of the date the election was made and from which period it is applicable. The Australian Taxation Office (2017g: online) states that the “annual private apportionment” adjustment will either increase the amount of Goods and Services Tax due to the Australian Taxation Office or decrease the refund due to the “small business entity”. In terms of section 131(45) of the Australian GST Act, the “annual private apportionment adjustment” is calculated as the input tax portion not attributable to a taxable purpose. In terms of section 131(20) of the Australian GST Act the “annual private apportionment adjustment” ceases when the taxpayer revokes the choice, or the Commissioner disallows the election.

3.2.6.3 PAYING GOODS AND SERVICES TAX BY QUARTERLY INSTALMENTS

In terms of section 162(5) of the Australian GST Act a taxpayer may elect to pay Goods and Services Tax by quarterly instalments if the following criteria are satisfied:

- the taxpayer is a “small business entity” as defined for “income year” in which the election is made; or
- the taxpayer is not carrying on a business and the enterprise’s Goods and Services Tax turnover is AUD 2m or less (for example, a not-for-profit organisation); and
- the taxpayer does not submit activity statements on a monthly basis or an alternative basis as determined by the Commissioner;
- if the taxpayer has previously submitted Goods and Services Tax returns on a monthly basis, at least four continuous months returns were submitted in the previous “income year”;
- all previous Goods and Services Tax returns were submitted;
- the taxpayer is not in a net refund position in the preceding year; and
- the taxpayer is a non-resident that “redelivers offshore supplies”, makes “inbound intangible supplies” or “supplies low value goods connected to an indirect tax zone”.

3.2.7 INVESTORS IN SMALL BUSINESS - EARLY STAGE VENTURE CAPITAL LIMITED PARTNERSHIP INVESTMENT

Section 360(10) of the Australian Income Tax Act states that the concession for early stage investors (effective from 1 July 2016) was introduced to assist “small Australian innovation companies with high-growth potential”. In terms of section 360(25) an investor will obtain a tax offset of twenty percent of the amount invested, limited to AUD200 000 for an “income year”, and section 360(50) states that the investor may disregard capital gains where the shares were held for a continuous period of more than twelve months but less than ten years. A capital loss will be disregarded where the shares are held for a continuous period of less than ten years.

In terms of section 360(15) the concession is available to an investor that satisfies the following criteria:

- a natural person, partnership, trust or private company;
- issued with shares in an “early stage innovation company” which is not an “affiliate” of the investor;
- the share issue does not represent an employee share scheme; and
- “immediately after the investment” the investor does not hold more than thirty percent of the equity interest in the company (or a connected company).

A member of a trust, partnership or a trustee will be entitled to the concession where the trust or partnership is entitled to the concession or the trustee is an individual and the trust is liable to pay tax on the trust’s net income. In terms of section 360(20) the concession will not be available where the investor was issued with shares and a disclosure document was required in terms of the Australian Corporations Act, and the investor paid more than AUD50 000 for the shares.

Section 360(40) states that an “early stage innovation company” is:

- incorporated in Australia within the last three “income years” or within the last six income years and in the last three income years the expenditure of the company and wholly owned subsidiaries did not exceed AUD1m;
- the expenses of the company and its wholly owned subsidiaries do not exceed AUD1m in the previous “income year”;
- the “assessable income” of the company and wholly owned subsidiary did not exceed AUD200 000;
- the company is not listed on a stock exchange; and
- the company scores 100 points on the innovation test in terms of section 360(45) of the Australian Income Tax Act or the company is focussed on and can demonstrate innovation.

Section 118(407) of the Australian Income Tax Act states that an Early Stage Venture Capital Limited Partnership provides an investment vehicle for both Australian and foreign limited

partners to invest in early stage and growth companies. The requirements to qualify as an Early Stage Venture Capital Limited Partnership are as follows:

- the partnership's committed capital should be between AUD10m and AUD200m;
- the partnership should follow an approved investment plan;
- investments should be made in unlisted entities;
- repurchase of investments from partners should not exceed twenty percent of the committed capital; and
- the total asset value of the "early stage innovation company" should not exceed AUD50m.

The Australian Taxation Office (2017h: online) points out that the Early Stage Venture Capital Limited partnership is taxed on a flow through principle and the limited partners bear the tax consequences. Section 51(52) of the Australian Income Tax Act states that the capital and revenue profits on disposal and income earned by limited partners (both local and foreign), will be exempt from tax. Distributions received by general partners will be taxed as capital in nature and not on revenue account. In terms of section 118(407) of the Australian Income Tax Act, where the individual owned the early stage venture capital investment for at least twelve months, the capital gain or loss on disposal of the investment will be disregarded.

The Department of Industry, Innovation and Science (2017: online) explains that the Venture Capital Limited Partnership rules allow a foreign investor to be exempt from capital gains tax when disposing of their investment held for at least twelve months. It appears that there is no specific indication that the Venture Capital Limited Partnership relief is available to Australian investors in small business in Australia, but rather to stimulate foreign investment in Australia. Therefore, the Venture Capital Limited Partnership regime is excluded from the scope of this thesis.

3.2.8 ADMINISTRATIVE CONCESSIONS

There are limited administrative concessions available for a "small business entity". A "small business entity" will be entitled to a Pay As You Go (PAYG) concession and a concession in respect of amending their assessment.

3.2.8.1 PAY AS YOU GO CONCESSION

In terms of section 45 of the Tax Administration Act, No. 1 of 1953 (Australian Tax Administration Act) taxpayers receiving business or trading income must settle their expected income tax liability by means of periodic payments. A “small business entity” has a liability to make quarterly PAYG payments in terms of section 45(130) of the Australian Tax Administration Act but may elect that the Australian Taxation Office determines the amount of PAYG that is due. The amount is determined with reference to previous assessable income information provided to the Australian Taxation Office, adjusted for business growth.

3.2.8.2 AMENDMENT OF ASSESSMENTS

Section 328(10)(2), read with section 170 of the Australian Income Tax Act provides that a “small business entity” has a two-year period from the date the Commissioner issued the assessment to request an amendment to an assessment issued by the Commissioner.

3.3 NEW ZEALAND

The Ministry of Business, Innovation and Employment (2017: online) reveals that ninety seven percent of all enterprises in New Zealand could be classified as a small business. These small businesses employ twenty-nine percent of the work force and contribute twenty six percent to the New Zealand Gross Domestic Product. EY (2016: online) points out that “small businesses play a critical role in the New Zealand economy”.

3.3.1 THE DEFINITION OF A SMALL BUSINESS IN NEW ZEALAND

The Ministry of Business, Innovation and Employment (2017: online) explains that a small business in New Zealand is defined as a business that employs less than twenty employees. It appears that there is no official tax definition for a small business in New Zealand. It can be concluded where reference is made to small businesses it refers to a business that employs less than twenty employees, unless a small business definition is provided for the specific concession.

3.3.2 INCOME TAX INCENTIVES AVAILABLE TO SMALL BUSINESSES IN NEW ZEALAND

New Zealand provides a range of incentives, including fringe benefit tax, provisional tax and Pay As You Earn (PAYE) concessions, accounting for financial arrangements on the cash basis and a number of goods and services tax concessions.

3.3.2.1 FRINGE BENEFIT TAX CONCESSIONS

Inland Revenue (2006a: online) points out that the “fringe benefit tax” concessions should assist small and medium sized businesses with their cash flow and reduce compliance costs.

3.3.2.1.1 OPTIONS FOR PAYMENT OF FRINGE BENEFIT TAX

In terms of section RD26 of the Income Tax Act No. 97, of 2007 (the New Zealand Income Tax Act), an employer is liable for “fringe benefit tax” when the employer provides an employee with a “fringe benefit”. Section CX2 of the New Zealand Income Tax Act defines a “fringe benefit” as a “benefit provided by an employer to an employee in connection with their employment” and it is either an unclassified benefit or the provision of:

- the private use of a motor vehicle;
- subsidised transport;
- employment-related loans;
- services for members and former members of Parliament; or
- contributions to life or health insurance.

Section RD61 of the New Zealand Income Tax Act provides that a “small-business person” may elect to pay “fringe benefit tax” on an annual basis. For the purposes of the “fringe benefit tax” concession in terms of section RD61 of the New Zealand Income Tax Act, a “small-business person” is defined in terms of section RC40 of the New Zealand Income Tax Act as:

... a person who —

- (a) conducts a business on their own account, acting alone or as a partner in

- a partnership; and
- (b) does not use a company or a trust in the conduct of the business; and
- (c) derives income that is mainly from the business, and does not consist of interest, dividends, royalties, rent, or beneficiary income.

In terms of section RD 61 of the New Zealand Income Tax Act, the “fringe benefit tax” concession will only be available to a “small-business person” where the “small-business person provides a fringe benefit to an employee” and the employee is not a shareholder in the “small-business person” in a “tax year”. Furthermore, “for the preceding tax year tax obligations for employment-related taxes” should not exceed NZD1m or the “small-business person” did not employ any employees during the preceding “tax year”. A “tax year” is defined as the period from 1 April to 31 March in terms of section YA1 of the New Zealand Income Tax Act.

Where a “small-business person” elects to pay “fringe benefit tax” on an annual basis, section RD61 provides that the Commissioner must be informed of the election by 30 June in the relevant “tax year” or on the last day of the quarter where the “small-business person” first starts employing employees.

Section RD61 states that the “fringe benefit tax” is calculated as “49.25% of the taxable value of a fringe benefit” or with reference to “the total pay of each employee”. Where the “small-business person” operates two or more businesses at the same time or ceases a current business and commences with a new business, the amounts of tax withheld must be aggregated.

3.3.2.1.2 FRINGE BENEFIT TAX – CLOSE COMPANY OPTION

Section RD60 of the New Zealand Income Tax Act applies where a “close company” provides a “fringe benefit” to an employee that holds shares in the “close company”. The “close company” may elect to pay the “fringe benefit tax” on an annual basis.

A “close company” is defined in section YA1 of the New Zealand Income Tax Act as a company where one of the following requirements is satisfied:

- a maximum of five natural persons holds more than fifty percent of the voting rights;

- a maximum of five natural persons holds more than fifty percent of the market value of the shares; and
- the company is not a special corporate entity as defined in section YA1 of the New Zealand Income Tax Act.

The requirements of the “close company option” are contained in section RD60 of the New Zealand Income Tax Act and the provisions of section RD60 will apply where a “close company” provides a “fringe benefit” to an employee that holds shares in the “close company” and in the “preceding income year”:

- tax obligations for employment-related taxes did not exceed NZD1m;
- the only “fringe benefit” provided was the “personal use of a motor vehicle” to an employee that holds shares in the “close company” and a maximum of two motor vehicles were provided; or
- the close company did not employ any employees.

The calculation of the “fringe benefit tax” and the administrative provisions is similar to the provisions contained in section RD60 of the New Zealand Income Tax Act, discussed in paragraph 3.3.2.1.1 above.

3.3.2.1.3 FRINGE BENEFIT TAX – UNCLASSIFIED BENEFITS

In terms of section YA1 of the New Zealand Income Tax Act an “unclassified benefit” is defined as a benefit not specifically provided for in terms of the New Zealand Income Tax Act. Section RD45 of the New Zealand Income Tax Act provides that an employer does not have to account for “fringe benefit tax” on “unclassified benefits” where the “taxable value” of the “unclassified benefits”:

- does not exceed NZD22 500 for the “income year”;
- where the employer pays “fringe benefit tax” on a quarterly basis, the “taxable value” does not exceed NZD300 per employee; or
- where the employer pays “fringe benefit tax” on an annual basis, the “taxable value” does not exceed NZD1 200 per employee.

3.3.2.2 PROVISIONAL TAX CONCESSIONS

A small business in New Zealand may be entitled to an early payment discount, the use of the Goods and Services Tax ratio to determine provisional tax payment and the relief of interest on the underpayment of provisional tax.

3.3.2.2.1 PROVISIONAL TAX EARLY PAYMENT DISCOUNT

An “early payment discount” refers to “a discount of income tax” in terms of sections RC38 and RC39 of the New Zealand Income Tax Act. Section RC39 of the New Zealand Income Tax Act provides that the early payment discount is treated as a payment of income tax and the early payment discount is credited against the “small business person’s” income tax account. In terms of section RC37 of the New Zealand Income Tax Act, this concession is available to a “small business person” (as discussed in paragraph 3.3.2.1.1 above) that is not required to pay “provisional tax” for the “income year” and has never received an “early payment discount” or been liable to pay “provisional tax” in the preceding four income years.

In terms of section RC38 of the New Zealand Income Tax Act, the early payment discount is calculated as the lesser of:

- 6.7% of the income tax paid for the “income year”; or
- 105% of the “residual income tax” for the “income year”.

The terms “income year” and “residual income tax” are defined in section YA1 of the New Zealand Income Tax Act. An “income year” refers to the “tax year”, which ends on 31 March or an alternative period approved by the Commissioner. “Residual income tax” represents the income tax payable less any Pay As You Earn (PAYE) and the relevant tax credits the taxpayer may be entitled to. Section RC38 of the New Zealand Income Tax Act states that the concession will apply where the “small business person” satisfies the following requirements:

- income tax is paid on or before the end of the financial year;
- the taxpayer has a credit on the income tax account of at least the lesser of:
 - income tax paid on or before the end of the financial year; or

- the amount of income tax liability;
- the tax year corresponds to the income year (i.e. 31 March); and
- the taxpayer has applied for the “early payment discount”.

3.3.2.2.2 PROVISIONAL TAX – GOODS AND SERVICES TAX RATIO OPTION

In terms of section RC16 a person liable for provisional tax may elect the Goods and Services Tax ratio in calculating their provisional tax liability if the requirements in terms of RC16 are satisfied. For the preceding tax year:

- the residual income tax should be more than NZD2 500 but not exceeding NZD150 000;
- the person is registered for Goods and Services Tax in the current and previous tax year; and
- the ratio percentage (residual income tax divided by total taxable supplies) calculated by Inland Revenue is between 0% and 100%.

For the current year, the person should be registered to submit GST returns on a monthly or two-monthly basis. The provisional tax payments will be made on a two-monthly basis together with the Goods and Services Tax payments.

It appears this may assist small business, but the requirement to be registered on a monthly or two-monthly basis is contrary to the Goods and Services Tax relief available for small business to submit GST returns every six months as discussed in paragraph 3.3.5.1.3.

3.3.2.2.3 PROVISIONAL TAX AND THE USE OF MONEY INTEREST

Section 120KE of the Tax Administration Act, No 166 of 1994 (the New Zealand Tax Administration Act), states that where a taxpayer uses the standard uplift method of calculating their provisional tax payment and their “residual income tax” is less than NZD60 000, interest on the underpayment of their tax liability will only be levied from the date when the last payment is due. The concession will be available where the taxpayer did not use an estimation

or the Goods and Services Tax ratio method to determine their provisional tax payment and there is no provisional tax interest avoidance arrangement.

3.3.2.3 DEDUCTION FOR LEGAL EXPENSES

In terms of section DB62 of the New Zealand Income Tax Act, where the taxpayer's total "legal expense" for the "income year" does not exceed NZD10 000, the legal expenditure is deducted in full, irrespective whether it is capital in nature or not. For the purposes of this provision, "legal expenses" is defined as expenditure for "legal services" rendered by a person "who holds a practising certificate issued by the New Zealand Law Society or an Australian equivalent". The Inland Revenue (2009: online) notes that this concession will enable taxpayers to deduct the "legal expenses" without having to distinguish between capital and revenue expenditure.

3.3.2.4 VALUATION OF CLOSING STOCK LESS THAN NZD10 000

In terms of section EB23 of the New Zealand Income Tax Act taxpayers may use the value of their opening trading stock as the value of their closing trading stock in an "income year" where the following requirements are satisfied:

- the taxpayer's "turnover" does not exceed NZD1 300 000 in an "income year"; and
- the taxpayer can "reasonably estimate that the value of the closing stock at the end of the 'income year' is less than NZD10 000".

Section YA1 of the New Zealand Income Tax Act defines "turnover" as the total trading income for the "income year" but excluding the value of closing stock.

3.3.2.5 PAY AS YOU EARN CONCESSIONS

3.3.2.5.1 PAY AS YOU EARN ONCE-A-MONTH FILING AND PAYMENT

In terms of sections RD22 of the New Zealand Income Tax Act, an employer would normally have to pay PAYE twice a month. Section RD22 of the New Zealand Income Tax Act states that an employer may qualify to pay over PAYE to Inland Revenue on a monthly basis, where

the requirements in terms of section RD22 are satisfied. Section RD22 requires that the employer should not be a new employer and that the gross amount of “tax obligations for employment-related taxes” is less than NZD500 000. The “tax obligations for employment-related taxes” includes both payments in respect of PAYE and “employer superannuation cash contributions”.

3.3.2.5.2 PAY AS YOU EARN INTERMEDIARIES

In terms of section RP4 of the New Zealand Income Tax Act, “the Commissioner may pay a subsidy to a listed PAYE intermediary for a payroll service that they provide to an employer”, provided that:

- the employer’s “tax obligations for employment-related taxes” is less than NZD500 000 for the “tax year”;
- the intermediary and taxpayer signed a contract for the rendering of the service;
- the intermediary has assumed the responsibility for making PAYE and superannuation contribution payments; and
- submits the correct “subsidy claim form”.

Paragraph 4 of the Income Tax (Payroll Subsidy) Regulations 2006 (Inland Revenue, 2006b: online) states that the subsidy paid to the PAYE intermediary amounts to NZD2 per employee per day, up to a maximum of five employees.

The Inland Revenue (2015: online) has indicated that the PAYE intermediary scheme should alleviate the small employer’s administrative burden and allow the small employer to grow their business.

3.3.2.5.3 CAPITAL ALLOWANCES – ITEMS OF LOW VALUE

In terms of section EE38 of the New Zealand Income Tax Act, a taxpayer may elect to deduct the full cost of an asset in the “income year” the asset was acquired, if the following requirements are satisfied:

- the total cost does not exceed NZD500;
- the asset is in use or available for use;
- the asset does not form part of any other depreciable assets (it is a standalone item);
- a deduction is denied in terms of another section of the New Zealand Income Tax Act; and
- where the item forms part of a group of items purchased from the same supplier at the same time with the same depreciation rate, the total cost of the group of items does not exceed NZD500.

3.3.2.6 FINANCIAL ARRANGEMENTS

In terms of section EW1 of the New Zealand Income Tax Act, the purpose of the financial arrangements provisions is to account for the income and expenditure over the term of the “financial arrangement”. Section EW3 of the New Zealand Income Tax Act defines a “financial arrangement” as debt or a similar instrument. Section EW55 of the New Zealand Income Tax Act states that a taxpayer may elect to account for a “financial arrangement” on the cash basis instead of over the term of the arrangement. Therefore, in terms of the cash basis, the taxpayer will not be taxed on amounts that were not actually received. The following requirements in terms of section EW54 read with section EW57 must be satisfied to elect the cash basis:

- the absolute value of the income and expenditure of all financial arrangements for a taxpayer in an “income year” does not exceed NZD100 000; or
- the absolute value of all financial arrangements for a taxpayer does not exceed NZD1m at any given time in an “income year”; and
- the difference between the accrual and cash basis does not exceed NZD40 000.

3.3.3 CAPITAL GAINS TAX CONCESSIONS

It appears that there are no Capital Gains Tax concessions for small businesses in New Zealand.

3.3.4 NEW ZEALAND INCOME TAX RATE

In terms of section YA1 read with Schedule 1, part A to the New Zealand Income Tax Act, a company has a flat tax rate of twenty eight percent. It appears that New Zealand does not have a reduced income tax rate applicable to small businesses.

3.3.5 GOODS AND SERVICES TAX CONCESSIONS

3.3.5.1.1 REGISTRATION THRESHOLD

In terms of section 51(1) of the Goods and Services Tax Act, No. 141 of 1985 (the New Zealand GST Act), a person is liable to register for Goods and Services Tax where the total value of their supplies exceeds or is reasonably expected to exceed NZD60 000 in a twelve-month period. The Inland Revenue (2009: online) indicates that the registration threshold will result in lower Goods and Services compliance cost and that a person may still voluntarily register for Goods and Services Tax even though their supplies are below the threshold of NZD60 000.

3.3.5.1.2 ACCOUNTING FOR GOODS AND SERVICES TAX ON THE PAYMENT BASIS

In terms of section 19A of the New Zealand GST Act, the following persons may apply to register for Goods and Services Tax on the payment basis:

- a non-profit body or a non-resident that is registered for Goods and Services Tax; or
- a person whose taxable supplies did not exceed or are not reasonably expected to exceed NZD2m in a twelve-month period; or
- the Commissioner is satisfied that based on the “nature, volume, and value of taxable supplies ... and the nature of the accounting system” the payment basis would be suitable for the person.

3.3.5.1.3 FILING OF GOODS AND SERVICES TAX RETURNS

Section 15 of the New Zealand GST Act states that a registered person must submit the Goods and Services Tax returns on a six monthly, two monthly or on a monthly basis. A person may apply to the Commissioner for the six-monthly submission period, if the following requirements are satisfied:

- the taxable supplies have not exceeded and is not reasonably expected to exceed NZD500 000 in a twelve-month period; or
- at least eighty percent of the taxable supplies are made within a maximum period of six months during the “income year” which concludes on the last day of the “income year” or within one month of the end of the “income year”; and
- the person was not previously registered for the six-monthly Goods and Services return submission for the twenty-four months prior to the application.

3.3.6 INVESTORS IN SMALL BUSINESS

In terms of EX37 of the New Zealand Income Tax Act, where a non-resident venture capital investor holds a share in an unlisted New Zealand resident company for at least twelve months, but for less than ten years, the proceeds on disposal of the investment will be exempt from tax.

It appears that there is no specific indication that this relief is available to New Zealand investors in small business in New Zealand, but rather to stimulate foreign investment in New Zealand.

3.3.7 ADMINISTRATIVE CONCESSION - ONGOING MONTHLY PENALTY

In terms of section 139B(2A) of the New Zealand Tax Administration Act, the ongoing monthly one percent penalty for outstanding tax debt will no longer apply to new debt in the following circumstances:

- Goods and Services Tax for periods ending on or after 31 March 2017;
- provisional tax and income tax commencing from the 2018 “income year”; or

- “Working for Families tax credit overpayments for the 2017–18 or later income years.”

3.4 SINGAPORE

The Department of Statistics Singapore (2016: online) has drawn attention to the fact that small and medium sized enterprises (comprising: companies, businesses, non-profit organisations, ministries and statutory boards) make up ninety-nine percent of the total enterprises in Singapore. Furthermore, small and medium sized enterprises employ sixty-five percent of the work-force and contribute forty-seven percent to the nominal value added.

3.4.1 THE DEFINITION OF A SMALL, MEDIUM AND MICRO-SIZED ENTERPRISE IN SINGAPORE

The Standards, Productivity and Innovation Board Singapore (n.d.: online) states that to qualify as a small and medium enterprise, the annual turnover should not exceed SGD100m, or no more than 200 people should be employed by the enterprise. Iqbal and Rahman (2015: 260) report that the definition of a small, medium and micro enterprise is characterised by its annual turnover as illustrated in [Table 3.1](#) below.

Table 3.1: Small, Medium and Micro Enterprises in Singapore

| Classification | Annual Turnover |
|-----------------------|------------------------|
| Micro | ≤ SGD 1m |
| Medium | > SGD 1m – SGD 10m |
| Small | > SGD 10m – SGD 100m |

Source: Iqbal and Rahman (2015: 260)

It is submitted that where reference is made to small businesses this refers to businesses with an annual turnover that does not exceed SGD100m, unless a small business definition is provided for the specific concession.

3.4.2 INCOME TAX INCENTIVES FOR SMALL BUSINESSES IN SINGAPORE

Singapore provides a range of tax incentives, including a start-up tax exemption scheme, a partial tax exemption for existing businesses, a double deduction for internationalisation, a productivity and innovation credit, carry back of losses and capital allowances and a number of goods and services tax concessions.

3.4.2.1 START-UP TAX EXEMPTION SCHEME

In terms of section 43(6A) of the Singapore Income Tax Act Chapter 34, ordinance 39 of 1947 (the Singapore Income Tax Act) a “qualifying company” will obtain a 100% tax exemption on the first SGD100 000 of normal “chargeable income” and a further fifty percent tax exemption on the next SGD200 000 of “chargeable income” for the “first three years of assessment” beginning on or after the 2008 “year of assessment”. Hawksford (n.d.: online) asserts that the start-up exemption scheme will significantly reduce the effective income tax rate for small and medium sized companies in Singapore.

Section 43(10) of the Singapore Income Tax Act provides that a “qualifying company” is defined as a company:

- incorporated in Singapore;
- that is a tax resident in Singapore for the “year of assessment”; and
- that does not have more than twenty shareholders and where those shareholders are individuals, the shares are beneficially held in their own names or at least one individual shareholder beneficially holds at least ten percent of the ordinary shares issued by the company.

A company limited by guarantee may be considered to be a “qualifying company” in terms of section 43(10) of the Singapore Tax Act where all the members are individuals or at least one of the individuals has contributed ten percent or more of the total contributions made by members for “basis period” in that “year of assessment”.

In terms of section 2(1) of the Singapore Income Tax Act, a “year of assessment” means “the period of 12 months commencing on 1st January 1948, and each subsequent period of 12 months”. According to the Inland Revenue Authority of Singapore (2017a: online) the “year of assessment” is the year in which a person’s “income is assessed to tax”. Section 2(1) further defines the “basis period” for any “year of assessment” as the financial year (the twelve-month period preceding the “year of assessment”). “Chargeable Income” is defined in terms of section 38 of the Singapore Tax Act as the remainder of income assessable to tax after the allowable “reliefs and deductions” have been made.

In terms of section 43(10) the “first three years of assessment” refers to “basis period” in which the company is incorporated and the following consecutive two years, immediately following the first year of assessment.

The Inland Revenue Authority of Singapore (2017a: online) points out that companies with the principal activity of investment holding, property development for investment or resale will not be entitled to the start-up company tax exemption scheme.

3.4.2.2 PARTIAL TAX EXEMPTION FOR COMPANIES

In terms of section 43(6) of the Singapore Income Tax Act, every company or body of persons is entitled to the partial tax exemption for companies, provided that the company did not utilise the start-up tax exemption in terms of section 43(6A) of the Singapore Income Tax Act. Section 43(6)(a) of the Singapore Income Tax Act indicates that companies may only utilise the partial tax exemption for the 2008 year of assessment and subsequent years of assessment.

Section 43(6)(i) of the Singapore Income Tax Act provides that seventy-five percent of the first SGD10 000 “chargeable income” is exempt from tax; section 43(6)(ii) states that fifty percent of the next SGD290 000 of the “chargeable” income is exempt from tax. Therefore, the maximum exemption for a “year of assessment” will be SGD152 500. Hawksford (n.d: online) asserts that the partial tax exemption scheme will reduce the effective income tax rate for small and medium sized companies in Singapore significantly.

3.4.2.3 CORPORATE INCOME TAX REBATE

In terms of section 92E of the Singapore Income Tax Act, a company may be entitled to a tax rebate for the 2016 and 2017 “year of assessment” that is equal to the lower of 50% of the corporate tax payable or SGD50 000. Hawksford (n.d.: online) explains that the corporate income tax rebate was raised from thirty percent to fifty percent for the 2016 and 2017 years of assessment to especially assist small and medium sized enterprises. The Inland Revenue Authority (2017b: online) has drawn attention to the fact that the corporate income tax rebate will be extended to the 2018 “year of assessment”. The rebate will be the lower of twenty percent of corporate tax payable or SGD10 000.

3.4.2.4 DOUBLE TAX DEDUCTION FOR INTERNATIONALISATION

International Enterprise Singapore (n.d.: online) explains that the double tax deduction for internationalisation is aimed at small and medium sized enterprises, as these businesses are encouraged to internationalise. In terms of section 14K, read with section 14B of the Singapore Income Tax Act, a Singapore resident company or an approved firm that carries on business in Singapore may obtain a double tax deduction (capped at SGD100 000) for “qualifying expenses” for the following “qualifying activities”:

- trade fair, exhibition, mission or promotion held or conducted outside Singapore;
- an approved trade fair held in Singapore;
- expenses in maintaining an approved trade office;
- market development expenditure for the carrying out of marketing activities.

Expenditure in excess of SGD100 000 in a “year of assessment” will require approval by International Enterprise Singapore.

Section 14 of the Singapore Income Tax Act provides that expenditure will only be deductible from income to the extent that it is “wholly and exclusively incurred ... in the production of income”. In terms of section 14KA of the Singapore Income Tax Act, salaries will be allowed as a double deduction up to SGD1m per “year of assessment” from 1 July 2015 to 31 March 2020 for Singapore citizens working in an entity abroad.

3.4.2.5 PRODUCTIVITY AND INNOVATION CREDIT

The Ministry of Finance Singapore (n.d.: online) asserts that the Productivity and Innovation Credit was introduced to allow small business to increase productivity and produce innovative business ideas. In terms of section 37I of the Singapore Income Tax Act a taxpayer may be entitled to a non-taxable cash pay-out of forty percent of the expenditure incurred in any of the six qualifying activities. The non-taxable cash pay-out is capped at SGD100 000 for the year of assessment.

The six qualifying activities are:

- research and development;
- purchase and licensing of Intellectual Property Rights;
- registration of Intellectual Property Rights;
- product or industrial design carried out in Singapore; and
- purchase or leasing of equipment or software for employee skills development and automation processes.

Section 37C of the Singapore Income Tax Act allows for the deduction of 400% of the expenditure in relation to the qualifying activities (as discussed above) up to a maximum of SGD400 000. This cap is raised to SGD600 000 for small businesses. This concession will expire at the end of the 2018 year of assessment. A taxpayer may either elect the cash pay-out or the 400% deduction of the expenditure.

3.4.2.6 CARRY BACK OF LOSSES AND CAPITAL ALLOWANCES

In terms of section 37H of the Singapore Income Tax Act, a taxpayer may “carry-back” the unutilised capital allowances and trade losses from the current “year of assessment” to the immediate preceding “year of assessment”. The amount will be deducted in the immediate preceding “year of assessment” limited to SGD100 000. The unutilised capital allowances will be deductible before the trade loss. The taxpayer will need to lodge a claim with the Inland Revenue Authority of Singapore to utilise this concession. In addition, section 37H states that the shareholding from the beginning of the “year of assessment” to the end of the “year of assessment” in which the capital allowances were claimed, or the loss incurred, should not

change by more than fifty percent. Substantially the same business should be carried on in the current “year of assessment” as the business carried on in the immediate preceding “year of assessment”. This concession will not be available to taxpayers where the income is wholly exempt from tax, derived from investment trades or where provisions of the Singapore Income Tax Act limit unutilised capital allowances and trade losses.

3.4.3 CAPITAL GAINS TAX INCENTIVES

The Inland Revenue Authority (2017c: online) points out that there is no capital gains tax in Singapore.

3.4.4 CORPORATE TAX RATE

In terms of section 43(1) of the Singapore Income Tax Act, the headline corporate income tax rate is seventeen percent. Hawksford (n.d.: online) states that the competitive corporate income tax rate is attractive to small and medium sized businesses. It appears that there is no reduced tax rate applicable to small and medium sized businesses in Singapore.

3.4.5 GOODS AND SERVICES TAX CONCESSIONS

3.4.5.1.1 REGISTRATION THRESHOLD

In terms of section 9(1) read with paragraph 1 of the First Schedule to the Goods and Services Tax Act, No. 31 of 1993 (the Singapore GST Act) a “person” must register for Goods and Services Tax where the “taxable turnover” exceeds or is likely to exceed SGD1m in a twelve-month period. Paragraph 8(1) of the First Schedule to the Singapore GST Act provides that a “person” may register voluntarily for General Sales Tax, if the “person” remains registered for a period of at least two years in terms of paragraph 8(2) of the First Schedule to the Singapore Goods and Services Tax Act.

3.4.5.1.2 CASH ACCOUNTING SCHEME

The Inland Revenue Authority of Singapore (2016: 14) points out that the “Cash Accounting Scheme” was introduced to assist small businesses with their cash flow. Regulation 68 of the Goods and Service Tax (General) Regulations (Ministry of Finance Singapore, 2008: online), stipulates that a “taxable person” that has voluntarily registered for Goods and Services Tax in terms of paragraph 8 of the First Schedule to the Singapore Goods and Service Tax Act may account for “output tax” when the cash is received and claim “input tax” when payment is made. Regulation 69 (Ministry of Finance Singapore, 2008: online), provides that a “taxable person” must apply for approval in terms of the “Cash Accounting Scheme”, subject to the provisions contained in Regulation 69. In terms of Regulation 70 (Ministry of Finance Singapore, 2008: online), the approval will be valid for a period of two years from the date the approval takes effect.

3.4.6 INVESTORS IN SMALL BUSINESS

3.4.6.1.1 INVESTMENT IN A START-UP COMPANY

In terms of section 37K of the Singapore Income Tax Act, a “qualifying person” investing in new shares of a “qualifying start-up company” from 1 July 2010 to 31 March 2020 may obtain a deduction for the investment. A “qualifying person” is an individual who incurred expenditure to acquire shares in a start-up company and held the shares for a continuous period of two years. The individual will be eligible to deduct fifty percent of the investment made in the “year of assessment” in which the two-year period ends. The investment may not exceed SGD500 000; therefore, the maximum deduction will be SGD250 000 for an investment. The “qualifying investor” is required to make a minimum investment of SGD100 000. In addition, the deduction will only be granted for investments made after approval was granted by the Minister and the Minister “is satisfied the individual possesses the necessary experience, skills, or expertise to nurture and grow a qualifying start-up company”.

A “qualifying Start-up Company” is:

- not limited by guarantee;
- unlisted and incorporated in Singapore for a maximum of three years;
- no shareholder is a relative of a “qualifying person” at the date of the first investment;
- a maximum of twenty individuals may hold more than fifty percent of the shareholding;
- the qualifying person and their relatives may not hold more than twenty five percent of the issued shares during the two-year holding period; and
- during the holding period the company does not engage in an activity that may be specified by the Minister.

3.4.7 ADMINISTRATIVE CONCESSION – SIMPLIFIED RECORD KEEPING

The Inland Revenue Authority of Singapore (2017b: online) points out that a business not registered for Goods and Services Tax may maintain a simpler form of records. The IRAS e-Tax Guide: Simplified record keeping for small businesses (Inland Revenue Authority of Singapore, 2013: 2) makes it clear that a small business for the purposes of the simplified record keeping is:

- a business that has annual revenue of less than SGD100 000 for the immediate preceding two financial years;
- at the last day of the “year of assessment” the business assets do not exceed SGD100 000;
- the business is not an investment holding or property development company; and
- the business is a sole proprietor or partnership that is not registered for Goods and Services Tax.

The Inland Revenue Authority of Singapore (2013: 3) has indicated that a small business must keep the following records:

- daily revenue and purchases records;
- monthly business expenses and employee remuneration records; and
- daily transport expense records.

3.5 IRELAND

The European Commission (2016: online) indicates that small and medium sized businesses account for 99.8% of the number of enterprises, employ 66.8% of persons employed and contribute 57.4% to Ireland's Gross Domestic Product. The European Commission (2016: online) points out that small and medium sized businesses are characterised by turnover *or* balance sheet total *and* the staff headcount. The European Commission divides small businesses in three categories, namely: medium-sized, small and micro.

Table 3.2: Small, Medium and Micro Enterprise in Ireland

| Company Category | Revenue | Balance Sheet | Staff Headcount |
|------------------|----------|---------------|-----------------|
| Medium-Sized | ≤ EUR 50 | ≤ EUR 43 | < 250 |
| Small | ≤ EUR 10 | ≤ EUR 10 | < 50 |
| Micro | ≤ EUR 2 | ≤ EUR 2 | < 10 |

Source: European Commission (2016: online)

3.5.1 INCOME TAX INCENTIVES FOR SMALL BUSINESSES IN IRELAND

Ireland provides a range of tax incentives, including a start-up tax exemption for new companies, start-up relief for the long term unemployed, an earned income credit, a surcharge on undistributed income, a research and development credit, reduced tax rates, capital gains tax and value-added tax concessions.

3.5.1.1 CORPORATION TAX EXEMPTION FOR NEW START-UP COMPANIES

In terms of section 486C of the Taxes Consolidation Act No 39 of 1997 (the Irish Income Tax Act), a newly incorporated company may qualify for the corporation tax exemption for the first three years of trading. The following requirements must be satisfied to utilise the relief:

- the company is incorporated in the European Economic Area on or after 14 October 2008;
- it commenced a “qualifying trade” between 1 January 2009 and 31 December 2018;
- and

- the total corporation tax in any one year should not exceed EUR40 000.

The exemption is applicable to income and gains on the disposal of assets from a “qualifying trade”. A “qualifying trade” is defined in terms of section 486C as a trade that does not include any of the following:

- an existing trade or a trade carried on previously;
- land development;
- exploration or extraction of petroleum and minerals;
- associated company’s trade carried on as part of the newly formed company; or
- activities including services, fishery, aquaculture, coal and agricultural products.

The exemption is calculated as the lower of EUR40 000 or the total Pay Related Social Insurance paid by the employer for all the employees. For the purposes of the exemption, the maximum Pay Related Social Insurance per employee amounts to EUR5 000. The unutilised portion of the relief may be carried forward after the three-year period, to be utilised in subsequent periods. The exemption will not be applicable to a company utilising the concession and commencing a new trade or where part of the trade is transferred to a connected person.

In terms of section 472AA of the Irish Income Tax Act, an individual starting a “new business” may be exempt from income tax for two years up to a maximum of EUR40 000 if the following requirements are satisfied prior to the commencement of the business:

- the individual was unemployed for at least twelve months; and
- received social assistance during the period of unemployment.

The period of unemployment includes periods spent on government training courses. The “new business” must satisfy the following requirements in terms of section 472AA:

- it must be an unincorporated entity set up from 25 October 2013 to 31 December 2018;
- it must be set up by the previously unemployed individual; and
- the business may not be bought, inherited or acquired.

3.5.1.2 EARNED INCOME TAX CREDIT

In terms of section, 472AB of the Irish Income Tax Act an individual earning income from a trade or profession will be entitled to the “earned income tax credit”, which amounts to the lesser of twenty percent of the “qualifying income”, or EUR950. The “qualifying income” refers to income received from a trade of profession and does not include income subject to Pay As You Earn (PAYE). Where an individual earns PAYE Income as well as income from a trade or profession, the maximum total credit for both the PAYE and earned income tax credit combined is EUR1 650.

3.5.1.3 SURCHARGE ON UNDISTRIBUTED INCOME

Section 440 of the Irish Income Tax Act states that a “close company” is subject to an additional corporation tax (a “surcharge”) of twenty percent where the after-tax investment and rental income (passive income) is not distributed within eighteen months after the end of the accounting period. A trading company can reduce its undistributed passive income by 7.5% before calculating the twenty percent “surcharge”. The “surcharge” is not applied where the undistributed amount does not exceed EUR2 000.

In terms of section 441 of the Irish Income Tax Act, an incorporated professional company is liable for a “surcharge” of:

- fifteen percent on half of the undistributed professional income; and
- twenty percent of the undistributed passive income.

3.5.1.4 RESEARCH AND DEVELOPMENT CREDIT

In terms of section 766 of the Irish Income Tax Act, a taxpayer is entitled to a refundable credit of twenty-five percent of the research and development expenditure:

- which was not funded by any grants;
- carried out in the European Economic Area; and
- the expenditure is not deductible in another jurisdiction.

The tax credit is deducted against the corporation tax liability of a company. The company is entitled to the tax credit whether the research and development is carried out by the company, a university or a third party. The research and development expenditure credit applies in addition to the deduction of the expenditure, and the credit must be claimed within twelve months of the end of the year in which the expenditure was incurred.

Where the research and development is undertaken on behalf of the company by a university in the European Economic Area, the credit is the greater of:

- five percent of the total research and development expenditure; or
- EUR100 000.

Where a third party has undertaken the research and development and the company has informed the third party in writing that the company will claim the research and development expenditure, the credit is the greater of:

- fifteen percent of the total research and development expenditure; or
- EUR100 000.

In terms of section 766A of the Irish Income Tax Act, research and development expenditure relating to a building used for research and development will be taken into account for the credit as well, if the building is used at least thirty-five percent of the time for research and development purposes over a period of four years.

3.5.1.5 KNOWLEDGE DEVELOPMENT BOX

In terms of section 769I of the Irish Income Tax Act, profits from intellectual property as it relates to research and development may be taxed at an effective rate of 6.25%. The effective tax rate is achieved by deducting fifty percent of the “qualifying profits” calculated as a percentage of the Research and Development expenditure and the profits that arise from the assets used for research and development.

Section 769R of the Irish Income Tax Act expands the definition of “intellectual property” for small, medium and micro enterprises, to include “inventions that are certified by the Controller

of Patents, Designs and Trade Marks as being novel, non-obvious and useful”. Section 769R stipulates the following additional requirements for small, medium and micro enterprises to be eligible for the 6.25% corporation tax on intellectual property profits:

- income from intellectual property does not exceed EUR7 500 000;
- where the taxpayer is a member of a group, the total group turnover does not exceed EUR50m; and
- the taxpayer is a small, medium or micro sized business as defined.

This relief is available from 1 January 2016 to 31 December 2020.

3.5.1.6 CAPITAL GAINS TAX CONCESSION - ENTREPRENEUR RELIEF

In terms of section 597AA of the Irish Income Tax Act, the capital gain on the disposal of “chargeable business assets” will be subject to a ten percent capital gains tax rate, up to a maximum lifetime limit of EUR1m. The reduced capital gains tax rate compares favourably to the normal capital gains tax rate of thirty-three percent, in terms of section 28 of the Irish Income Tax Act. A “chargeable business asset” is an asset used for business purposes, including goodwill, but excluding:

- the holding of shares or investments;
- the holding of development land; or
- development or letting of land.

The assets must be disposed of at least three years after the date of purchase and owned by the individual for at least a continuous period of three years out of the five years immediately prior to disposal, for a taxpayer to be eligible for the relief.

Where an individual carries on a business through a private company and a disposal is made by a private company, the individual may be entitled to the entrepreneur relief, if the individual holds at least five percent of the equity shares in the private company or five percent in a holding company that holds a hundred percent of the private company. The individual should be employed by the company or serve as a director in a technical or managerial position for a

continuous period of three out of the immediately preceding five years prior to disposal. The individual should spend at least fifty percent of their time in the technical or managerial role, while being employed. The shareholding of the abovementioned individual is specifically included in the definition of a “chargeable business asset”; therefore, if the individual disposes of their shareholding, the disposal is within the ambit of section 597AA.

The entrepreneur relief is not available to:

- disposals by companies;
- disposals of development land;
- rental assets;
- a disposal which does not give rise to a chargeable gain;
- assets owned by the individual but used by a company in their trade; or
- the holding of investments.

3.5.1.7 CORPORATE INCOME TAX RATE

In terms of section 21 of the Irish Income Tax Act, the corporate income tax rate on trading profits in Ireland is 12.5%, but non-trading income (passive income) is taxed at 25% in terms of section 21A of the Irish Income Tax Act. It appears that there is no specific small business tax rate in Ireland.

3.5.2 VALUE-ADDED TAX

In terms of section 74 of the Value-Added Tax Consolidation Act 2010 (Irish VAT Act) a person accounts for VAT on the invoice basis. Section 80 of the Irish VAT Act provides that VAT may be accounted for on money received in the following circumstances:

- more than ninety percent of the “accountable person’s” turnover is derived from supplies made to persons not registered for VAT; or
- the “accountable person’s” total turnover does not exceed EUR2m in a continuous period of twelve months.

The Department of Finance (2013: online) has indicated that the increase in the threshold will assist small businesses with their cash flow. The compulsory VAT registration threshold for the supply of services is EUR37 500 in terms of section 6(1)(d) of the Irish VAT Act and EUR75 000 for the supply of goods or the supply of goods and services, in terms of section 6(1)(c) of the Irish VAT Act.

3.5.3 INVESTORS IN SMALL BUSINESSES

3.5.3.1 EMPLOYMENT AND INVESTMENT INCENTIVE SCHEME

In terms of section 490 of the Irish Income Tax Act a “qualifying individual” may deduct expenditure incurred to acquire “qualifying shares” in a “qualifying company” before 31 December 2020. The individual is entitled to deduct a maximum of EUR150 000 from total income in any one tax year, provided the minimum investment is EUR250.

The requirements to be satisfied before qualifying for the concession are extensive and outside the scope of this thesis. The key elements: “qualifying individual”; “qualifying shares” and a “qualifying company” are discussed below.

Section 492 of the Irish Income Tax Act defines a “qualifying individual” as an investor that:

- is an Irish tax resident for the tax year in which the deduction is claimed;
- obtains the shares in the “qualifying company” for their own behalf; and
- is not a connected person to the company.

In terms of section 488 of the Irish Income Tax Act, “qualifying shares” are paid up ordinary shares with no preferential rights. In terms of section 494 of the Irish Income Tax Act, a “qualifying company” is an unlisted, small, medium or micro enterprise, which is tax resident in Ireland. Section 489 of the Irish Income Tax Act states that the deduction from income is provided for as follows:

- thirty-fortieths in the year of assessment the shares are issued; and

- ten-fortieths in the tax year following the third anniversary of the investment, provided that the company increased employment levels and expenditure on Research and Development during the three years the shares are held.

3.5.3.2 START-UP REFUNDS FOR ENTREPRENEURS (SURE)

The Irish Tax Institute (2014: online) points out that the Seed Capital Scheme has been rebranded as the “Start-up Refunds for Entrepreneurs”. In terms of section 493 of the Irish Income Tax Act an individual who obtains shares in a new company will be entitled to deduct the investment against their income for any of the preceding six years prior to the year in which the investment was made. The deduction may not exceed EUR100 000 per tax year and EUR600 000 in total. The relief is available for investments made up to 31 December 2020. In addition, the following requirements must be satisfied:

- the individual must be a full-time employee or director of the new company for up to six months after the tax year in which the business was established;
- at least seventy-five percent of the individual’s income must be employment income, and other sources of income may not exceed EUR50 000 in each of the three years prior to being employed by the new company;
- the individual is not entitled to own more than fifteen percent of another company, unless the turnover did not exceed EUR127 000 in the three years prior to the investment and the company’s trade did not constitute financial services or trading in land;
- the individual acquires fifteen percent or more of the newly established company and holds the investment for the longer of one year from the date of investment or commencement of trade; and
- the permissible trades for the new company must be of an employment creation nature.

3.5.3.3 CARRIED INTEREST

In terms of section 541C of the Income Tax Act, where a partnership, company or individual receives their share of profits from the management of a venture capital fund the profits may be subject to a tax concession. The requirements to be satisfied are as follows:

- the profits received from the unquoted shares or shares in a private trading company should not exceed twenty percent of the venture capital fund profits;
- the investors in the venture capital fund should be limited or general partners;
- the investors should be obliged by means of an agreement to provide lump sums for investment;
- investments should be made in unquoted shares or private trading companies for at least three years; and
- the investee should be involved in research and development, telecommunication, business processes and scientific or new technology.

The return on the investment is taxed as a chargeable gain for capital gains tax purposes and is provided for in the form of a fifteen percent capital gains tax rate for an individual or partnership and a 12.5% capital gains tax rate for a company.

3.6 CONCLUSION

This chapter has identified what constitutes a small business in Australia, New Zealand, Singapore and Ireland, outlined the incentives available to small businesses in these selected jurisdictions and the relief available to investors in small business. [Table 3.3](#) provides an overview of the incentives available in the various jurisdictions.

In addressing the research goal, the following chapter will identify and compare the similarities and differences in the tax incentives available to small, medium and micro-sized enterprises, and investors in these businesses in South Africa, to those available in Australia, New Zealand, Singapore and Ireland, to identify possible measures that could be implemented in South Africa.

Table 3.3: Tax Incentives available in Australia, New Zealand, Singapore and Ireland

| Definition / Incentives | Australia | New Zealand | Singapore | Ireland |
|---------------------------------|--|---|--|---|
| A small business is defined by: | Turnover of < AUD10m. | A business that employs less than twenty employees. | Turnover of \leq SGD100m <i>or</i> a maximum of 200 employees. | Revenue \leq EUR50m <i>or</i> a balance sheet total \leq EUR43m <i>and</i> < 250 employees. |
| Income and Expenditure: | <ul style="list-style-type: none"> • immediate deductibility of capital and revenue start-up expenditure; • change in trading stock value not accounted for where change \leq AUD5 000; and • prepaid expenditure may be deducted in “income year” incurred. | <ul style="list-style-type: none"> • change in trading stock value not accounted or where change \leq NZD10 000; and • financial arrangements accounted for on the cash basis. | <ul style="list-style-type: none"> • double tax deduction for internationalisation; and • carry back of losses and capital allowances. | <ul style="list-style-type: none"> • No small business specific income and expenditure incentives. |
| Capital Allowances: | <ul style="list-style-type: none"> • low value items (< AUD20 000) deductible in full; and • cost \geq AUD20 000 depreciated as one asset in “small business pool”. | <ul style="list-style-type: none"> • Low value items (< NZD500) deductible in full | <ul style="list-style-type: none"> • Carry back of losses and capital allowances to the immediate preceding year of assessment. | <ul style="list-style-type: none"> • No small business specific capital allowance incentives. |
| Provisional Tax: | <ul style="list-style-type: none"> • No small business specific Provisional Tax incentives. | <ul style="list-style-type: none"> • early payment discount; • election to pay Provisional Tax on Goods and Services | <ul style="list-style-type: none"> • No small business specific Provisional Tax incentives. | <ul style="list-style-type: none"> • No small business specific Provisional Tax incentives. |

| | | | | |
|---------------------|---|--|---|---|
| | | <p>Tax ratio as determined by the Commissioner; and</p> <ul style="list-style-type: none"> • interest on underpayment only levied from the date last payment is due. | | |
| Employees' Tax: | <ul style="list-style-type: none"> • No small business specific Employees' Tax incentives. | <ul style="list-style-type: none"> • monthly filing and payment; and • the use of PAYE intermediaries. | <ul style="list-style-type: none"> • No small business specific Employees' Tax incentives. | <ul style="list-style-type: none"> • No small business specific Employees' Tax incentives. |
| Fringe Benefit Tax: | <ul style="list-style-type: none"> • car parking exemption; and • work-related device exemption. | <ul style="list-style-type: none"> • employer election to pay tax on annual basis; • close company election to pay tax on annual basis; and • no fringe benefit tax on "unclassified benefits". | <ul style="list-style-type: none"> • No small business specific Fringe Benefit Tax incentives. | <ul style="list-style-type: none"> • No small business specific Fringe Benefit Tax incentives. |
| Capital Gains Tax: | <ul style="list-style-type: none"> • 15-year asset exemption; • 50% active asset reduction; • retirement exemption; • rollover exemption; and • restructure of small business exemption. | <ul style="list-style-type: none"> • No small business specific Capital Gains Tax concessions. | <ul style="list-style-type: none"> • There is no capital gains tax in Singapore. | <ul style="list-style-type: none"> • Entrepreneur relief for "chargeable business assets". |
| Tax Rate: | <ul style="list-style-type: none"> • 27.5% for a "small business entity". | <ul style="list-style-type: none"> • No reduced tax rate for small businesses. | <ul style="list-style-type: none"> • No reduced tax rate for small businesses. | <ul style="list-style-type: none"> • surcharge (15% to 20%) on undistributed |

| | | | | |
|---|--|--|--|---|
| | | | | <p>passive income earned by a “close company”;</p> <ul style="list-style-type: none"> • profits from intellectual property taxed at 6.25%; and • no reduced tax rate for small businesses. |
| Rebates / Tax offset / Tax Exemptions: | <ul style="list-style-type: none"> • A maximum of AUD1 000 set-off against tax on small business income portion. | <ul style="list-style-type: none"> • No reduced tax rate for small businesses. | <ul style="list-style-type: none"> • start-up tax exemption for the first three years for new companies; • partial tax exemption for companies; • corporate income tax rebate; and • productivity and innovation credit. | <ul style="list-style-type: none"> • corporation tax exemption for new start-up companies for the first three years; • start-up relief (tax exemption) for long-term unemployed; • earned income credit; and • research and development credit. |
| Goods and Services Tax / Value-Added Tax: | <ul style="list-style-type: none"> • cash basis of accounting; • annual apportionment of input tax; and • quarterly instalments. | <ul style="list-style-type: none"> • NZD60 000 registration threshold; • payment basis of accounting; and • bi-annual return submissions. | <ul style="list-style-type: none"> • SGD1m registration threshold; and • cash basis of accounting. | <ul style="list-style-type: none"> • Value-Added Tax accounted for on the money-received basis. |
| Investors: | <ul style="list-style-type: none"> • Early Stage Venture Capital Investors exempt from capital gains tax and eligible for tax offset of 20% of investment capped at AUD200 000. | <ul style="list-style-type: none"> • No specific relief for investors in small business. | <ul style="list-style-type: none"> • Deduction for direct investment in start-up companies capped at a maximum of SGD250 000. | <ul style="list-style-type: none"> • employment and investment incentive scheme deduction for direct investment in small business; • tax deduction for employees or directors |

| | | | | |
|-----------------|--|---|--|---|
| | | | | <p>purchasing share in a new company (Start-Up Refunds for Entrepreneurs); and</p> <ul style="list-style-type: none"> • return on a venture capital investment taxed as a capital gain and not as revenue. |
| Administrative: | <ul style="list-style-type: none"> • Pay as You Go (periodic payments); and • assessments may amended for up to two years after the assessment was issued. | <ul style="list-style-type: none"> • Ongoing monthly penalty on new tax debt waived. | <ul style="list-style-type: none"> • Simplified record keeping. | <ul style="list-style-type: none"> • No small business specific administrative incentives. |

Source: Author

CHAPTER 4: COMPARISON OF SMALL BUSINESS TAX CONCESSIONS

4.1 INTRODUCTION

In addressing one of the sub-goals of the research, this chapter compares the tax concessions available to small, medium and micro-sized enterprises, and investors in these businesses in South Africa, to those available in Australia, New Zealand, Singapore and Ireland. The purpose of this comparison is to identify similarities, differences, and possible measures that could be introduced in South Africa. The discussion in this chapter will address the following aspects in relation to small, medium and micro-sized enterprises:

- the definition of a small business for tax purposes;
- the tax incentives available for small, medium and micro-sized enterprises; and
- the tax incentives available to investors in small, medium and micro-sized enterprises.

To ensure that monetary thresholds are comparable, the following exchange rates were applied when making comparisons.

Table 4.1: Exchange rates

| Foreign Currency | Exchange Rate (R) |
|------------------|-------------------|
| AUD1 | 10.7037 |
| NZD1 | 9.48639 |
| SGD1 | 10.0896 |
| EUR1 | 16.1862 |

Source: XE (2017: online)

4.2 THE SMALL, MEDIUM AND MICRO-SIZED ENTERPRISE DEFINITION

Evans *et al* (2014: 456) submit that “there is no universally accepted definition of a small business. Moreover, the definition of a small business for the purpose of tax concessions may vary even within the same jurisdiction between taxes”. It appears that the jurisdictions included

in this study use any one or a combination of the following factors to determine whether an entity will qualify as a small business:

- turnover;
- balance sheet total; or
- staff headcount.

Where a turnover threshold is applied, [Table 4.2](#) below illustrates the thresholds per jurisdiction.

Table 4.2: Small business turnover threshold

| Jurisdiction | Annual Turnover | Entity Type |
|--------------|--|-----------------------------|
| South Africa | ≤ R20 000 000 | Small Business Corporation |
| | ≤ R1 000 000 | Micro Business |
| Australia | < R107 037 000 (AUD10m x R10.7037) | Small Business Entity |
| New Zealand | no turnover requirement | |
| Singapore* | ≤ R1 008 960 000 (SGD100m x R10.0896) | Small and Medium Enterprise |
| Ireland** | R809 310 000 (EUR50m x R16.1862) | Medium-sized business |
| | ≤ R161 862 000 (EUR10m x R16.1862) | Small business |
| | ≤ R32 372 400 (EUR2m x R16.1862) | Micro business |

Source: author

* Singapore applies either the turnover *or* the staff headcount as a threshold.

**Ireland applies the combination of turnover *or* balance sheet total *and* the staff headcount as a threshold.

New Zealand defines a small business in terms of the number of people employed as opposed to a monetary threshold and classifies a small business as a business where less than twenty people are employed. Singapore defines a small business either by a turnover threshold (as per [Table 4.2](#)) *or* the number of people employed. The indications are therefore that a business in Singapore will qualify as a small business where a maximum of 200 people are employed or where the turnover is below R1 008 960 000. Ireland applies the combination of turnover *or* balance sheet total *and* the staff headcount as a threshold. The balance sheet total and staff headcount requirement is illustrated in [Table 4.3](#) below.

Table 4.3: Ireland – balance sheet total and staff headcount

| Company Category | Balance Sheet | Staff Headcount |
|-------------------------|---------------------------------------|------------------------|
| Medium-Sized | ≤ R696 006 600 EUR43m x R16.1862 | < 250 |
| Small | ≤ R161 862 000 (EUR10m x R16.1862) | < 50 |
| Micro | ≤ R 32 372 400 (EUR2m x R16.1862) | < 10 |

Source: European Commission (2016: online)

It is clear therefore, that the small business thresholds in South Africa are significantly below the monetary thresholds in Australia, Singapore and Ireland.

When considering any additional requirements to be classified as a small business, New Zealand, Singapore and Ireland do not have any additional requirements. Australia requires that a business be operated for an “income year” as a sole trader, partnership, company or trust. Like Australia, South Africa requires a “micro business” to be operated as a sole-trader or a company. In contrast, South Africa has a complex list of requirements for a business to be classified as a “small business corporation”:

- a legal entity requirement;
- a holder of shares requirement;
- a “gross income” requirement; and
- a business activity requirement.

It appears that the international jurisdictions follow an approach of a single requirement for a business to be classified as a small business. It is submitted that the South African National Treasury should consider increasing the monetary threshold for the turnover requirement of a “micro business” and “small business corporation”. Furthermore, a single requirement approach is suggested (turnover, staff headcount and/or balance sheet total) to reduce the additional onerous and complex requirements to be classified as a “small business corporation” in South Africa.

It appears that certain small business incentives must satisfy different thresholds before the specific incentive is available to a small business. Where different criteria apply for a small

business to qualify for the concession, this will be discussed as part of the comparison of the incentives.

4.3 INCOME TAX INCENTIVES

A wide spectrum of income tax incentives were identified in the various jurisdictions, including simplified depreciation and methods for accounting for trading stock, as well as enhanced deductions for certain types of expenditure.

4.3.1 INCOME TAX INCENTIVES NOT RELATING TO CAPITAL ALLOWANCES

Other than the accelerated capital allowances for a “small business corporation”, there are no additional tax-deductible incentives for small businesses in South Africa.

Australia provides the following tax-deductible incentives for a “small business entity”:

- immediate deductibility of professional advice and services start-up expenditure, and the capital versus revenue distinction is not required for the start-up expenditure deduction;
- simplified trading stock rules where a “small business entity” is not required to conduct a stock take or account for the difference between the opening and closing stock in an “income year”, if the difference does not exceed R53 519 (AUD5 000 x R10.7037); and
- the immediate deduction of prepaid expenditure where the “eligible service period” does not exceed twelve months.

New Zealand provides the following tax-deductible incentives for small businesses:

- where the total legal expenses for the “income year” are R94 864 (NZD10 000 x R9.48639) or less, the legal expenditure is deductible in full, whether capital in nature;

- where the trading stock is valued at R94 964 (NZD10 000 x R9.48639) or less, the small businesses may use the opening stock value as the closing stock value; and
- “financial arrangements” may be accounted for on a cash received basis.

Singapore provides the following tax-deductible incentives for small businesses:

- a double tax deduction for internationalisation expenditure incurred on “qualifying activities”, capped at R1 008 960 (SGD100 000 x R10.0896), and salaries capped at R10 089 600 (SGD1m x R10.0896);
- a 400% deduction of expenditure incurred on “qualifying activities” relating to productivity and innovation, capped at R6 053 760 (SGD600 000 x R10.0896); and
- the carry back of losses and capital allowances to the immediate preceding “year of assessment” up to a maximum of R1 008 960 (SGD100 000 x R10.0896).

Clearly, South Africa and Ireland do not provide for similar tax-deductible incentives that are comparable to the incentives available in Australia, New Zealand and Singapore. It is submitted that the South African National Treasury should consider implementing enhanced tax deductions to assist small businesses (for example: simplified trading stock rules, the immediate deductibility of capital start-up expenditure and relaxing the prepaid expenditure anti-avoidance provision for a small business in South Africa).

4.3.2 FRINGE BENEFIT TAX CONCESSIONS

Australia introduced the following fringe benefit tax concessions for a “small business entity”:

- a car parking exemption, where an employer is not liable for “fringe benefit tax” if an employee is provided with a car parking facility; and
- no “fringe benefit tax” will be levied on a “portable electronic device” with effect from 1 April 2016.

New Zealand provides the following “fringe benefit tax” concessions for small businesses:

- a “small business person” as defined for the “fringe benefit tax” concession purposes may elect to pay “fringe benefit tax” on an annual basis as opposed to when the benefit is provided;
- where a “close company” provides a “fringe benefit” to an employee who holds shares in the “close company”, the “close company” may elect to pay the “fringe benefit tax” on an annual basis; and
- an employer does not have to account for “fringe benefit tax” on “unclassified benefits”, where the thresholds as discussed in paragraph 3.3.2.1.3 of chapter 3 are not exceeded.

By contrast, South Africa, Singapore and Ireland do not provide tax concessions in respect of fringe benefits provided to employees. It is submitted that the South African National Treasury may consider fringe benefit tax relief for small businesses in South Africa, to assist these small businesses with their cash flow and compliance costs.

4.3.3 CAPITAL ALLOWANCE CONCESSIONS

A “micro business” in South Africa does not have any capital allowance concessions, as a “micro business” pays tax on “taxable turnover”. A “small business corporation” will be entitled to deduct 100% of the cost of a manufacturing machine in the “year of assessment” the machine is brought into use. Non-manufacturing assets are written-off over a three-year period, fifty percent in year one, thirty percent in year two and twenty percent in year three. Where the non-manufacturing asset is regarded as a “small item” with a Value-Added Tax exclusive cost of less than R7 000, the taxpayer may elect to write off the full cost of the asset in the “year of assessment” the asset is brought into use.

Australia provides simplified depreciation rules for a “small business entity”:

- assets acquired between 15 May 2016 and 30 June 2018 with a cost of less than R214 074 (AUD20 000 x R10.7037) are deductible in full in the “income year” it is brought into use or “installed ready for use”; and

- the use of a “small business pool” to depreciate multiple assets with a cost of R214 074 or more as a single asset at fifteen percent in year one and thirty percent in each subsequent year.

New Zealand, Singapore and Ireland do not provide small businesses with specific capital allowance incentives.

It can be concluded that the South African “small business corporation” incentive is generous when compared to Australia, as the full cost is deductible for a manufacturing machine in the “year of assessment it is brought into use” and non-manufacturing assets are depreciated over three years. By contrast, the “small business entity” concession for items with a cost below R214 074 in Australia is more generous than the “small item” incentive in South Africa. It must be recognised, that the “small item” concession in South Africa is not specifically targeted at small businesses, but merely provides a “small business corporation” with a choice to deduct the cost of a non-manufacturing asset in the “year of assessment” it is brought into use.

On this basis, it is submitted that the South African National Treasury should consider introducing a “small business corporation” specific “small items” threshold.

4.3.4 PROVISIONAL TAX CONCESSIONS

In South Africa, the “micro business turnover tax” regime replaces the provisional tax obligations. Nevertheless, a “micro business” must make two compulsory interim payments and a voluntary third payment if required. The interim payments represent the prepayment of the turnover tax liability. A “small business corporation” in South Africa, is not entitled to provisional tax relief.

New Zealand provides an “early payment discount” to a “small business person”, which is treated as a payment of income tax where the income tax is paid on or before of the end of the financial year. This concession is available to a “small business person” not registered for provisional tax. A taxpayer may elect to pay provisional tax based on their Goods and Services Tax ratio, as calculated by Inland Revenue. This concession will entitle the taxpayer to make provisional tax payments on a two-monthly basis. Where a taxpayer uses the standard uplift

method to calculate provisional tax, interest will only be levied from the date the last payment is due, provided that the “residual income tax” does not exceed R569 183 (NZD60 000 x R9.48639).

By contrast, Australia, Ireland and Singapore do not provide provisional tax concessions for small businesses. It appears that the lack of provisional tax concessions in South Africa is comparable to Australia, Ireland and Singapore. Therefore, it is submitted that the South African National Treasury should consider waiving penalties and interest on the underpayment of provisional tax by small businesses in South Africa. This treatment appears to be comparable to the interest relief in New Zealand.

4.3.5 START-UP TAX INCENTIVES

South Africa, Australia and New Zealand do not provide for targeted start-up tax concessions for small businesses.

Singapore has a start-up tax exemption scheme, where a taxpayer will be 100% exempt from tax on the first R1 008 960 (SGD100 000 x R10.0896) and a further fifty percent tax exemption on the next R2 017 920 (SGD200 000 x R10.0896) for the first three “years of assessment”. Ireland provides for a corporation tax start-up tax exemption for newly incorporated companies for the first three years of trading. The exemption is only available for “qualifying trades” and is calculated as the lower of R647 448 (EUR40 000 x R16.1862) or the total Pay Related Social Insurance calculated as a maximum of R80 931 (EUR5 000 x R16.1862) per employee. In addition, an individual starting a “new business” may be exempt from income tax for two years up to a maximum of R647 448 (EUR40 000 x R16.1862).

It must be noted that in South Africa a “micro business” will not pay tax on the first R355 000 of “taxable turnover”, whereas a “small business corporation” does not pay tax on the first R75 750 of “taxable income”. The indications are therefore that the relief in South Africa is significantly below that of Singapore and Ireland. It is submitted that the South African National Treasury should consider a tax exemption scheme for start-up businesses in South Africa or alternatively increase the “taxable turnover” and “taxable income” threshold at which a small business will be liable for tax in South Africa.

4.3.6 OTHER TAX CONCESSIONS

Where a South African “micro business” pays a dividend to the beneficial owner of a share, the dividend will be exempt from dividends tax, provided that the total dividends paid does not exceed R200 000 in a “year of assessment”. By contrast, similar relief is not available to a “small business corporation” in South Africa or to small businesses in Australia, New Zealand, Singapore or Ireland.

Where after-tax investment and rental income (passive income) is not distributed within eighteen months after the end of the accounting period in Ireland, an additional corporation tax (a surcharge of undistributed income) of twenty percent is levied on the undistributed amount. Where the undistributed amount does not exceed R32 372 (EUR2 000 x R16.1862), the surcharge does not apply. No recommendation is made in this regard as the “micro business” and “small business corporation” regime contains anti-avoidance provisions relating to passive income.

4.3.7 EMPLOYEES’ TAX (PAY-AS-YOU-EARN) CONCESSIONS

New Zealand provides that an employer with “tax obligations for employment-related taxes” of less than R4 743 195 (NZD500 000 x R9.48639) may qualify to pay employees’ tax (PAYE) monthly, as opposed to twice a month. To alleviate the small employer’s administrative burden, a subsidy is paid to a listed PAYE intermediary for payroll services rendered to an employer. South Africa, Australia, Singapore and Ireland do not provide a specific small business PAYE concession. In terms of paragraph 2(1) of the Fourth Schedule to the South African Income Tax Act, PAYE is due monthly in South Africa and therefore the PAYE obligation is comparable to the relief available in New Zealand. It appears that outsourcing the payroll function to a PAYE intermediary may reduce the compliance cost for small businesses in South Africa. Therefore, it is submitted that the South African National Treasury may consider implementing a subsidy regime similar to that of New Zealand to ease the compliance burden for small businesses.

4.3.8 CAPITAL GAINS TAX CONCESSIONS

In South Africa, a “micro business” disregards the capital gain or loss on the disposal of an asset used mainly for business purposes, but fifty percent of the proceeds on the disposal of a capital asset is included in “taxable turnover”. It appears that there is no specific capital gains tax concession for a “small business corporation” as defined. Also, in South Africa, a taxpayer may be entitled to an R1.8m lifetime exemption of a capital gain or loss on the disposal of a “small business asset”.

Australia defines a “small business entity” for capital gains tax purposes as an entity that meets the basic conditions and has an “aggregated turnover” that does not exceed R21 407 400 (AUD2m x R10.7037). Australia offers a range of capital gains tax incentives to a “small business entity”:

- a capital gains tax exemption where an asset was owned for 15 years prior to the disposal of the asset;
- a fifty percent capital gains tax reduction on the disposal of an “active business asset”;
- a retirement relief up to a lifetime limit of R5 351 850 (AUD500 000 x R10.7037);
- a deferral of a capital gain where a replacement asset is purchased; and
- no tax liability where the ownership of “small business entity” assets are restructured without affecting the “ultimate economic ownership” of the assets.

Ireland provides a taxpayer with entrepreneur capital gains tax relief. In terms of the entrepreneur relief, the capital gains tax inclusion rate on the disposal of a chargeable business asset is ten percent up to a maximum lifetime limit of R16 186 200 (EUR1m x R16.1862). Singapore does not have capital gains tax and New Zealand does not provide for any small business capital gains tax relief.

The indications are therefore that the “small business asset” relief in South Africa is similar to the retirement relief available in Australia, but the lifetime limit in South Africa (R1.8m) is significantly lower than the lifetime limit (the equivalent of R5 351 850) in Australia. By contrast, the “micro business” capital gains tax concessions are unique to South Africa, as

South Africa is the only jurisdiction included in this study to have implemented a “turnover tax” system.

It is submitted that the South African National Treasury should consider implementing an entrepreneur capital gains tax relief, to encourage individuals to invest in new businesses, and increase the “small business” capital gains tax exemption lifetime threshold. Further relief similar to that of Australia should be considered to assist South African small businesses to reduce their tax liability on the disposal of business assets.

4.3.9 TAX RATE CONCESSIONS

Where a business is classified as a “small business corporation” in South Africa, the normal tax payable is calculated on the “taxable income” in terms of a progressive tax table. By contrast, a “micro business” is taxed on its “taxable turnover” in terms of a progressive tax table. Therefore, a small business in South Africa is not taxed at the corporate tax flat rate of 28%. Thus, for example, the tax rates for “micro businesses” and small business corporations are as follows:

Micro business

On a taxable turnover of R1 million (the maximum for qualification as a “micro business”): the tax liability is:

$R6\,650 + 3\% \times (R1\text{m} - R750\,000) = R14\,150$, thus a tax rate of 1.42%. If a taxable income to turnover ratio of 20% is assumed, thus taxable income of R200 000, the tax rate is 7.08%.

Small business corporation

On a taxable income of R550 000, the tax liability is R59 150, a tax rate of 10.75%. On taxable income exceeding R550 000, the normal company rate of 28% applies.

In Australia, a “small business entity” is taxed at a flat rate of 27.5% in comparison to the corporate tax rate in Australia of 30%. New Zealand has a flat corporate tax rate of 28%, while Singapore has a corporate tax rate of seventeen percent. It appears that neither New Zealand nor Singapore has a reduced or progressive income tax rate for small businesses. In Ireland, the corporate tax rate for trading income is taxed at 12.5%, while an entity’s passive income is

taxed at twenty five percent. In terms of the knowledge development box concession in Ireland, profits from intellectual property, as it relates to research and development, may be taxed at 6.25% by deducting fifty percent of the research and development profits as an expense.

Table 4.4: Comparison of corporate tax rates

| Jurisdiction | Corporate tax rate | Small business tax rate |
|---------------------|--|--------------------------------|
| South Africa | 28% | Refer to the example above |
| Australia | 30% | 27.5% |
| New Zealand | 28% | n/a |
| Singapore | 17% | n/a |
| Ireland | 12.5% (trading income) 25% (passive income) | n/a |

Source: Author

It appears that the progressive tax tables in South Africa provide a substantial benefit to taxpayers at the lower end of the small business thresholds, but as the taxable income increases and reaches the top end of the threshold (R20m), the lower flat rates used in Singapore and Ireland may be more beneficial to the taxpayer. A South African “micro business” benefits from the low tax rate applied on taxable turnover to calculate the normal tax payable for a “micro business”. The indications are that the international jurisdictions included in this study do not have a “micro business” tax regime.

Therefore, it could be concluded that a small business in South Africa benefits from the reduced tax rates and pays less tax than a non-small business taxpayer in South Africa. Similarly, it appears that the progressive tax rates are more beneficial than applying a low reduced flat rate of tax. It is submitted that the South African National Treasury should consider increasing the “micro business” and “small business corporation” thresholds. The increased thresholds will provide small businesses with a further measure of tax relief.

4.3.10 TAX LIABILITY CONCESSIONS

Australia provides a “small business entity” income tax offset (rebate), limited to R10 704 (AUD1 000 x R10.7037). For the purposes of this concession, a “small business entity” is a business with an “aggregated turnover” of less than R53 518 500 (AUD5m x R10.7037).

Singapore provides a partial tax exemption for companies not utilising the start-up tax exemption. In terms of the partial tax exemption, seventy-five percent of the first R100 896 (SGD10 000 x R10.0896) will be exempt and fifty percent of the next R2 925 984 (SGD290 000 x R10.0896) will be exempt; therefore, the maximum exemption will be R1 538 664 (SGD152 500 x R10.0896). Furthermore, Singapore provides a corporate tax rebate. The rebate is lower of fifty percent of the corporate tax payable or R504 480 (SGD50 000 x R10.0896) for the 2016 and 2017 years of assessment. For the 2018 year of assessment the rebate is the lower of twenty percent of the corporate tax payable or R100 896 (SGD10 000 x R10.0896). In terms of the Productivity and Innovation Credit concession, a company may elect to receive a non-taxable cash rebate of forty percent of expenditure incurred on “qualifying activities”. The rebate is capped at R1 008 960 (SGD10 000 x R10.0896). It must be noted that a taxpayer has the option to elect between the non-taxable cash rebate and deducting 400% of the expenditure incurred on “qualifying activities”.

Ireland provides the following tax credits to reduce the tax liability:

- an earned income credit at the lesser of twenty percent of “qualifying income” or R15 377 (EUR950 x R16.1862), where an individual receives PAYE income, the maximum rebate (PAYE credits and earned income credit) is R26 707 (EUR1650 x R16.1862); and
- a refundable research and development credit of twenty-five percent of the research and development expenditure.

South Africa does not provide for any targeted small business tax rebates. It is submitted that the South African National Treasury should consider possible tax rebates for small businesses in South Africa, which will stimulate entrepreneurship and employment.

4.4 VALUE-ADDED TAX CONCESSIONS

In South Africa, a registered “micro business” may voluntarily register for VAT and submit VAT returns on a bi-annual basis. A natural person or partnership consisting of only natural persons may register for VAT on the payment basis, where taxable supplies in the previous taxable period (twelve months) do not exceed R2.5m. The compulsory registration threshold in South Africa is R1m. There is no VAT concession for a “small business corporation” in South Africa.

Australia provides a compulsory Goods and Service Tax registration threshold of R802 779 (AUD 75 000 x R10.7037). An Australian “small business entity” is provided with the following Goods and Services Tax concessions:

- a cash basis of accounting;
- the annual apportionment of input tax for private use purposes; and
- paying Goods and Services Tax in quarterly instalments.

The Goods and Services Tax concessions in New Zealand relate to the following:

- the compulsory registration for Goods and Services Registration threshold is R569 182 (NZD 60 000 x R9.48639);
- an entity may account for Goods and Services Tax on the payment basis where the taxable supplies do not exceed R18 972 780 (NZD 2m x R9.48639); and
- where the taxable supplies do not exceed R4 744 195 (NZD 500 000 x R9.48639) an entity may submit the Goods and Services Tax returns on a bi-annual basis.

Singapore provides a compulsory Goods and Services Tax registration threshold of R10 089 600 (SGD 1m x R10.0896) and a cash accounting basis for Goods and Services Tax where an entity registered voluntarily. Ireland only provides a concession to account for VAT on the money-received basis. The requirement for the money received basis is that the turnover does not exceed R32 372 400 (EUR2m x R16.1862) in a continuous twelve-month period. This is in contrast to the compulsory registration threshold of R1 213 965 (EUR75 000 x R16.1862)

for the supply of goods or the supply of goods and services. The compulsory registration threshold for the supply of services only is R566 517 (EUR37 500 x R16.1862).

It can be concluded that South Africa provides limited VAT concessions for small businesses and, in comparison to the international jurisdictions, the compulsory registration threshold (R1m) is above that of Australia (R802 778) and New Zealand (R569 182), marginally below Ireland (R1 213 965), but significantly below Singapore (R10 089 600). It is submitted that there are notable VAT concessions relating to small businesses in the international jurisdictions included in this study pertaining to reduced VAT return submission requirements and a cash basis of VAT payment. South Africa provides for a bi-annual submission of VAT returns for a “micro business” voluntarily registered for VAT, which is similar to New Zealand. The distinct difference between South Africa and the international jurisdictions is that South African does not provide the cash basis of accounting for small businesses operating as a juristic person. The other notable difference is that Australia provides an annual apportionment for private use and a quarterly Goods and Services Tax instalment option.

It is submitted that the South African National Treasury should consider increasing the compulsory VAT registration threshold of R1m to assist small businesses in South Africa with their cash flow and compliance cost, as there are no VAT concessions available for small businesses in South Africa that are comparable to the international jurisdictions included in this study. Alternatively, the South African National Treasury should consider extending the bi-annual return submission and the election to be registered on the cash basis to a “small business corporation” in South Africa.

4.5 INVESTORS IN SMALL BUSINESSES

Section 12J of the South African Income Tax Act provides taxpayers with a 100% tax deduction for their investment in an approved venture capital company. Where taxpayers dispose of their venture capital shares within five years, the initial deduction will be recouped. South Africa does not provide tax concessions for the income derived from the venture capital company.

Australia provides investors in an Early Stage Innovation Company a tax offset (rebate) of twenty percent of their investment, limited to R2 140 740 (AUD200 000 x R10.7037). If the investment is held for a continuous period of more than twelve months, but less than ten years, the capital gain on disposal will be disregarded. A capital loss will be disregarded where the investment is held for a continuous period of less than ten years. In addition, income earned by the investors will be exempt from tax.

In an attempt to stimulate foreign investment in New Zealand, a non-resident venture capital investor who holds an unlisted share in a New Zealand resident company for at least twelve months, but less than ten years, will be exempt from tax on the disposal of their investment. Singapore provides for a deduction of fifty percent of the direct investment in a start-up company. The deduction is only allowed after holding the shares for a continuous period of at least two years and is capped at R2 522 400 (SGD250 000 x R10.0896).

Where an investment is made in a small, medium or micro-sized enterprise, Ireland provides the individual with a deduction up to a maximum of R2 427 930 (EUR150 000 x R16.1862) in any one tax year, provided that the minimum investment is R4 047 (EUR250 x R16.1862). Thirty-fortieths of the deduction is allowed in the year of assessment the shares are issued and the remaining ten-fortieths is allowed after the third anniversary of the investment, provided that the company increased employment and research and development levels. An individual obtaining shares in a new company may deduct the investment for any of the preceding six years prior to the year in which the investment was made, up to a cap of R1 618 620 (EUR100 000 x R16.1862) per year and R9 711 720 ((EUR600 000 x R16.1862) in total. Where investments are made by means of a venture capital fund, the return on investment (carried interest) is taxed as a capital gain at a fifteen percent capital gains tax rate for an individual and a 12.5% capital gains tax rate for a company.

It can be concluded that South Africa only provides a tax deduction for an investment in a venture capital company. By contrast, Australia provides a capped rebate for an investment in a Venture Capital Partnership and no capital gains tax liability on disposal of the investment, which is similar to the relief for a non-resident investor in New Zealand. Comparable to South Africa, Singapore provides a capped deduction, but for a direct investment in a start-up company. In a similar way, Ireland provides a capped deduction for a direct investment in a new or existing company.

It appears that the venture capital investment deduction in South Africa is generous in comparison to the other jurisdictions included in this study, as no cap is placed on the deduction. Therefore, it is submitted that the South African National Treasury should also consider a form of tax relief for investors making a direct investment in South African small businesses.

4.6 TAX ADMINISTRATION CONCESSIONS

In South Africa, a “micro business” has a reduced administrative burden of the retention of documentation for five years after the submission of the tax return and may make twice-yearly payments of PAYE, the Skills Development Levy and Unemployment Insurance Fund contributions. It appears that there are no administrative concessions for a “small business corporation” in South Africa.

The Australian Tax Administration Act provides that a “small business entity” may elect for the Australian Taxation Office to determine the quarterly Pay-As-You-Go tax obligation. A “small business entity” has two years from the date an assessment was issued to request an amendment of the assessment. The New Zealand Tax Administration Act states that the monthly ongoing penalty for outstanding tax will no longer apply to new tax debt. The Inland Revenue Authority of Singapore has introduced simplified record keeping for small businesses. It appears that Ireland does not have a specific tax administrative concession for small businesses.

It appears that there are limited tax administration concessions available for small businesses in South Africa. It is submitted that the South African National Treasury should consider extending the PAYE, Skills Development Levy and Unemployment Insurance Fund concessions to a “small business corporation”. Furthermore, the South African National Treasury should consider waiving or reducing the ongoing penalties and interest for small businesses in South Africa, in favour of a fixed once-off penalty.

4.7 CONCLUSION

This chapter has identified the differences and similarities between the South African tax provisions and those of the selected international jurisdictions, as they relate to:

- the definition of a small business for tax purposes;
- the tax incentives available for small, medium and micro-sized enterprises; and
- the tax incentives available to investors in small, medium and micro-sized enterprises.

South Africa is similar to the majority of the international jurisdictions included in this study in employing a turnover threshold to determine whether a taxpayer will qualify as a small business. It was found that the threshold employed in South Africa is significantly lower than that of the international jurisdictions, but that there are additional complex requirements to be satisfied before a business could be classified as a small business in South Africa.

The tax incentives employed in South Africa focus on enhanced capital allowances, a reduction of the tax rate, capital gains tax relief and reduced administrative requirements. By contrast, the international jurisdictions employed multiple tax incentives (concessions) to assist small businesses in various areas, ranging from:

- simplified depreciation and trading stock methods;
- start-up tax relief;
- tax exemptions;
- comprehensive capital gains tax exemptions; and
- limited tax administration relief.

South Africa only provides a tax deduction for an investment in small business through a venture capital company. By contrast, the international jurisdictions provide deductions or tax rebates for direct investments in small businesses as well as a venture capital company. In addition, relief is provided on the investment returns and upon the disposal of the investment after a specified holding period.

On this basis, it is recommended that the South African National Treasury should consider the following:

- increasing the monetary threshold for the turnover requirement for a “micro business” and “small business corporation”;
- reducing the complex requirements to be classified as a “micro business” or “small business corporation”;
- enhanced tax deductions to assist small businesses;
- small business fringe benefit tax relief;
- a specific small business “small items” capital allowance threshold;
- waiving penalties and interest on provisional tax payments by small businesses;
- a start-up tax incentive scheme;
- Pay-As-You-Earn concessions for “small business corporations”;
- a deduction for a direct investment in small businesses;
- tax relief on the investment return and disposal of the investment in small businesses;
- an entrepreneur capital gains tax relief;
- increasing the “small business” capital gains tax lifetime exemption threshold;
- increasing the “taxable turnover” and “taxable income” thresholds for calculating the tax payable;
- providing tax rebates to stimulate entrepreneurship and employment;
- introducing the cash basis of accounting for “small business corporations”; and
- waiving or reducing ongoing penalties and interest in favour of a fixed once-off penalty for small businesses.

In the following chapter, the research findings for this thesis will be discussed.

CHAPTER 5: CONCLUSION

5.1 INTRODUCTION

The purpose of this research was to compare the tax incentives available to small businesses and investors in small businesses in South Africa to those available in Australia, New Zealand, Singapore and Ireland, to identify possible measures to be introduced in South Africa.

In achieving this research goal, the following sub-goals were addressed:

- the definition of a small business for tax purposes;
- the tax incentives available for start-up and existing small businesses;
- the tax incentives available for investors in small businesses, either through a venture capital company or a direct investment in a small business; and
- the possible measures to be introduced in South Africa.

5.2 FINDINGS

In addressing the sub-goals, chapter 2 discussed the small business tax regime in South Africa, chapter 3 discussed the small business tax regime in Australia, New Zealand, Singapore and Ireland, and chapter 4 compared the small business regimes to identify similarities, differences and possible measures that could be introduced in South Africa.

5.2.1 THE DEFINITION OF A SMALL BUSINESS FOR TAX PURPOSES

Chapter 2 explains that a small business in South Africa is categorised as a “micro business” or a “small business corporation”. The distinction is made primarily based on the turnover of the taxpayer in conjunction with other parameters. The additional parameters for a “small business corporation” are classified into:

- a legal entity requirement;
- a holder of shares requirement;
- a “gross income” requirement; and

- a business activity requirement.

Chapter 3 introduced the small business requirements for the international jurisdictions included in this research. The international jurisdictions classify a taxpayer as a small business based on the taxpayer's turnover, staff headcount or balance sheet total. Australia defines a small business as a "small business entity", where turnover is less than AUD10m. New Zealand requires that a business employ less than twenty employees to be classified as a small business. Singapore classifies a small and medium-sized enterprise as an entity with an annual turnover of less than SGD100m *or* an entity that employs less than 200 people. Ireland adopts the European Commission's definition of a small business, which is defined by the annual turnover *or* balance sheet total *and* staff headcount. A small, medium and micro-sized entity in Ireland has a turnover of less than EUR50m, a balance sheet total of less than EUR43m and a staff headcount of less than 250 employees.

5.2.2 THE TAX INCENTIVES AVAILABLE FOR START-UP AND EXISTING SMALL BUSINESSES

Chapter 2 indicated that a South African "micro business" pays tax on its "taxable turnover", is exempt from Capital Gains Tax, may voluntarily register for VAT and has reduced record keeping requirements. A "small business corporation" may be entitled to accelerated capital allowances. Both a "micro business" and a "small business corporation" calculate the normal tax payable in terms of a progressive tax table. South Africa provides for "small business asset" relief where an individual disposes of an asset due to being at least 55 years old, ill health, disability, retirement or death. Furthermore, there is no targeted tax incentive or start-up incentive for small businesses in South Africa.

Chapter 3 explains the tax incentives available for small businesses in Australia, New Zealand, Singapore and Ireland. Australia provides a wide spectrum of tax incentives, including the immediate deduction of start-up expenditure, irrespective whether the expense is capital in nature. Simplified depreciation rules where multiple assets are combined in a "small business pool" and depreciated as one asset, and items of a low value (< AUD20 000) are deducted immediately. Where the change in value of trading stock does not exceed AUD5 000, the "small business entity" may elect not to account for the change. Furthermore, Australia

provides for a small business income tax offset, and the immediate deduction of prepaid expenditure where the service period does not exceed twelve months. The corporate tax rate for a “small business entity” in Australia is 27.5%. Goods and Services Tax concessions allow a small business to account for the Goods and Services Tax on the cash basis, an annual apportionment of input tax for private purposes and paying goods and services tax in quarterly instalments. Fringe Benefit Tax concessions are provided for car parking and work-related portable electronic devices. The Capital Gains Tax concessions provide relief for the disposal of business assets, a retirement relief and no tax consequences on the restructuring of a small business. Limited administrative concessions are provided in the form of periodic payments and the amendment of assessments. New Zealand provides a small business with an option to pay Fringe Benefit Tax on an annual basis and not having to account for Fringe Benefit Tax on “unclassified benefits”. Provisional tax relief is provided in the form of an early payment discount, where income tax is paid before or on the end of the financial year, an election, where the Commissioner may determine the provisional tax due in terms of a Goods and Services Tax ratio, and interest on the underpayment of provisional tax will only be levied from the date the last payment is due. Where the requirements are satisfied, legal expenditure is deductible in full, without distinguishing between capital and revenue expenditure. The change in the value trading of stock is not accounted for where the difference is less than NZD10 000. Employees’ Tax concessions allow a small business to file and pay employees’ tax monthly and utilise a Pay As You Earn intermediary. Financial arrangements are accounted for on the cash basis and assets of a low value (< NZD500) are deductible immediately. There are no specific small business Capital Gains Tax concessions in New Zealand or a small business reduced tax rate. Goods and Services Tax concessions are provided in the form of a higher registration threshold, accounting for Goods and Services Tax on the payment basis and filing a bi-annual return. A limited administrative concession provides that no interest be levied on new tax debt.

Singapore allows for start-up and partial tax exemptions for small businesses, a double tax deduction to promote the internationalisation of small businesses, a productivity and innovation credit, as well as the carry back of losses and unutilised capital allowances. There is no Capital Gains Tax in Singapore or a reduced tax rate for small businesses. Goods and Services Tax concessions allow for the cash accounting basis and an increased registration threshold. A simplified record keeping concession is provided for small businesses.

Ireland provides for a corporate tax exemption for three years for new start-up companies, an unemployed individual commencing with a new business will be exempt from income tax for two years, an earned income credit is provided for trade and professional income, and a research and development credit aims to stimulate research and development in small businesses. A Capital Gains Tax entrepreneur relief is provided to encourage the investment in new businesses. Although there is no specific small business tax rate in Ireland, profits from intellectual property are taxed at 6.25%. The Value-Added Tax concession allows for an increased turnover threshold and accounting for Value-Added Tax on the money received basis.

5.2.3 THE TAX INCENTIVES AVAILABLE FOR INVESTORS IN SMALL BUSINESSES

Chapter 2 indicated that the venture capital incentive in South Africa was introduced to provide small businesses with access to equity finance. An investor in a venture capital company will be entitled to a full deduction of the expenditure “actually incurred” in exchange for the issue of venture capital company shares. Where an investor disposes of the venture capital shares within five years, the deduction will be recouped. South Africa does not provide for tax relief for a direct investment in a small business.

Chapter 3 explains the tax incentives available for investors in small businesses in Australia, New Zealand, Singapore and Ireland. Australia provides an investor in an Early Stage Venture Capital Limited Partnership with a tax offset of twenty percent of the amount invested, limited to AUD200 000, and an investor may disregard the capital gain where the investment was held for a continuous period of more than twelve months, but less than ten years. New Zealand does not have a targeted regime for investors in small business, but rather exempts a non-resident venture capital investor from tax on the disposal of their investment, to stimulate foreign investment. Singapore provides a tax deduction for a direct investment in a start-up company, limited to a maximum deduction of SGD250 000. In Ireland, an investor may obtain a deduction for a direct investment in a small business that is tax resident in Ireland. The deduction is limited to EUR150 000 in any one tax year. A full-time employee or director who obtains shares in a new company may deduct the investment over the six years prior to the year in which the investment was made, limited to EUR100 000 per year and EUR600 000 in total.

5.2.4 POSSIBLE MEASURES TO BE INTRODUCED IN SOUTH AFRICA

Chapter 4 concluded that the South African National Treasury should consider increasing the monetary threshold for the turnover requirement of a “micro business” and “small business corporation”. Furthermore, a single requirement approach (turnover, balance sheet total or staff headcount) to evaluate whether a business qualifies as a “micro business” or a “small business corporation”, should be considered to reduce the current complex requirements.

With reference to the tax incentives, chapter 4 concluded that South Africa provides relief in the form of enhanced capital allowances, a reduction in the tax rate, capital gains tax relief and reduced administrative requirements. Nevertheless, the international jurisdictions employed multiple incentives to assist small businesses in the form of simplified depreciation and trading stock methods, start-up relief, tax exemptions, comprehensive capital gains tax exemptions and limited administrative relief.

The following additional relief measures are recommended for small businesses in South Africa:

- enhanced tax deductions to assist small businesses;
- small business fringe benefit tax relief;
- a specific small business “small items” capital allowance threshold;
- waiving penalties and interest on provisional tax payments by small businesses;
- a start-up tax incentive scheme;
- Pay-As-You-Earn concessions for “small business corporations”;
- an entrepreneur capital gains tax relief;
- increasing the “small business” capital gains tax lifetime exemption threshold;
- increasing the “taxable turnover” and “taxable income” thresholds for calculating the tax payable;
- providing tax rebates to stimulate entrepreneurship and employment;
- introducing the cash basis of accounting for “small business corporations”; and
- waiving or reducing ongoing penalties and interest in favour of a fixed once-off penalty for small businesses.

Chapter 4 concluded that the South African venture capital incentive is generous in comparison to the other jurisdictions, as no cap is placed on the amount deductible. It is submitted that a tax relief for investors making a direct investment in small business in South Africa should be considered, as well as a tax relief on the investment return and disposal of the investment in small businesses.

5.3 DAVIS TAX COMMITTEE, SMALL AND MEDIUM ENTERPRISES: TAXATION CONSIDERATIONS

The Davis Tax Committee report: *Small and Medium Enterprises: Second and Final Report* (2016: 5 – 9) made recommendations to the Minister of Finance in respect of tax policy proposals for small, medium and micro-sized businesses. Table 5.1 below summarises the recommendations and indicates whether National Treasury implemented the recommendations. Only recommendations that are within the scope of this thesis are considered.

Table 5.1: Davis Tax Committee recommendations

| Recommendation | Implementation through a tax legislation amendment |
|--|--|
| <p><i>Turnover Tax</i></p> <ul style="list-style-type: none"> • “Taxpayers should be allowed to elect to exit the Turnover Tax system on an annual basis”. • The taxation liability as determined in terms of the Turnover Tax system “should be discharged by way of an annual declaration made on, or before, 31 May each year”. • “... a separate voluntary disclosure programme for micro business should be implemented. Registration in terms of the Sixth Schedule should automatically result in the waiver of any arrear tax claims relating to the period prior to 1 March 2015”. • “SARS and National Treasury should investigate measures that require a micro business to be tax registered before they can make use of electronic payment facilities”. | <ul style="list-style-type: none"> • The Taxation Laws Amendment Act No 43, of 2014 removed the requirement for a “micro business” to be locked into the “turnover tax” regime for three years. • No proposed amendments were identified for the remainder of the recommendations. |

| | |
|--|--|
| <p><i>Small Business Corporations (SBCs)</i></p> <p>The Davis Tax Committee made three main recommendations:</p> <ul style="list-style-type: none"> • “Retain the current SBC allowance and accept the potential for abuse and the enforcement problems this will entail”. • “Remove the SBC incentive completely and redeploy the resource within the Department of Small Business Development or Department of Trade and Industry by way of targeted interventions. In this regard, it is noted that the Department of Small Business Development has recently received an annual budget of R3 billion”. • Replace the SBC incentive with a “Refundable Compliance Rebate system”. • In addition, the Davis Tax Committee pointed out “consideration should be given” to increase the current “small items” capitalisation threshold of R7 000 for small businesses. | <ul style="list-style-type: none"> • No proposed amendments were identified for any of the recommendations. |
| <p><i>Value-Added Tax</i></p> <ul style="list-style-type: none"> • “There appears to be no justification to raise the compulsory registration threshold”. • The current threshold for the payment basis is accepted. • Small businesses should be “allowed to adjust the VAT computation” where “debtors’ balances exceed ninety days”. • Tax refunds should be subject to time limits. • VAT returns and “data received from financial institutions” should be examined to identify the abuse of the small business regime. | <ul style="list-style-type: none"> • No proposed amendments were identified for any of the recommendations. |
| <p><i>Venture Capital Companies</i></p> <ul style="list-style-type: none"> • National Treasury should consider a tax incentive for angel investors. | <ul style="list-style-type: none"> • No proposed amendment was identified. |
| <p><i>Tax Administration</i></p> <ul style="list-style-type: none"> • “Progress with regard to the new SARS initiatives relating to the Small and Medium Enterprises sector should be closely monitored and evaluated”. | <ul style="list-style-type: none"> • It is submitted that the recommendation does not give rise to a tax policy change. |

Source: Author

It is submitted that the recommendations made by the Davis Tax Committee do not appear to address the need for fundamental tax concessions that will encourage the growth of small businesses in South Africa.

5.4 LIMITATIONS OF SCOPE

As this was a thesis of limited scope, the discussion of certain aspects was limited. The following areas were specifically excluded in terms of South African legislation as well as the equivalent legislation in Australia, New Zealand, Singapore and Ireland:

- the Customs and Excise Act No. 91, of 1964;
- the Employment Tax Incentive Act No. 26, of 2013;
- the Skills Development Levies Act No. 9, of 1999;
- the Unemployment Insurance Contributions Act No. 4, of 2002;
- section 23O: Limitation of deductions by small, medium or micro-sized enterprises in respect of amounts received or accrued from small business funding entities;
- section 30C: small business funding entities;
- small business tax amnesty;
- section 37G: determination of taxable income derived from small business undertakings;
- section 8F: interest on hybrid debt instruments deemed to be dividends in specie;
- section 10(1)(cQ): receipts and accruals of an approved small business funding entity in terms of section 30C;
- section 10(1)(zE): amounts received by or accrued to the Small Business Development Corporation limited, by way of any subsidy or assistance payable by the State;
- section 10(1)(zK): amounts received by or accrued to or in favour of a small, medium or micro-sized enterprise from a small business funding entity; and
- paragraph 63B of the Eighth Schedule to the South African Income Tax Act: Small business funding entities.

5.5 SUGGESTION FOR FUTURE RESEARCH

A suggestion for future research could include the tax implications of crowdfunding for both the receiver and the person making the pledge. The research could consider the various methods of crowd funding and its accompanying tax implications.

5.6 CONCLUSION

The introduction to this research identified that the small business concessions available to “micro businesses” and “small business corporations” in South Africa are “perceived as unfair” and “fundamentally ineffective”. The purpose of this research was to compare the tax incentives available to small businesses and investors in small businesses in South Africa to those available in Australia, New Zealand, Singapore and Ireland, to identify possible measures to be introduced in South Africa.

What the research has shown, is that South Africa has complex tax legislation for a business to be classified as a “micro business” or “small business corporation” and a limited number of tax concessions. In contrast, the international jurisdictions investigated in this research provide a simple classification of small businesses, associated with a wide range of tax concessions.

It is impossible to address the barriers faced by small business through tax legislation alone, but South Africa has an opportunity to simplify the tax legislation to alleviate one of the significant barriers faced by small businesses. It is submitted that amending the tax legislation may assist small businesses to grow and achieve the goals set out in the National Development Plan: simplifying the regulatory environment and providing access to finance. It can be concluded that it is not enough to merely provide the incentives; it requires a commitment to the growth of small businesses and the active involvement in the sector by government.

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Australian Legislation

Australian Income Tax Assessment Act, No. 38 of 1997, as amended.

Fringe Benefit Tax Assessment Act, No. 39 of 1986, as amended.

Goods and Services Tax Act, No. 55 of 1999, as amended.

Income Tax Assessment Act, No. 27 of 1936, as amended.

Tax Administration Act, No. 1 of 1953, as amended.

New Zealand Legislation

Goods and Services Tax Act, No. 141 of 1985, as amended.

Income Tax Act, No. 97, of 2007, as amended.

Tax Administration Act, No. 166 of 1994, as amended.

Ireland Legislation

Taxes Consolidation Act, No. 39 of 1997, as amended.

Value-Added Tax Consolidation Act 2010, as amended.

Singapore Legislation

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